

AMENDED IN SENATE MARCH 20, 2002  
AMENDED IN SENATE FEBRUARY 13, 2002  
AMENDED IN SENATE JANUARY 23, 2002  
AMENDED IN SENATE SEPTEMBER 14, 2001  
AMENDED IN SENATE JUNE 5, 2001  
AMENDED IN ASSEMBLY APRIL 4, 2001

CALIFORNIA LEGISLATURE—2001–02 REGULAR SESSION

## ASSEMBLY BILL

**No. 1122**

**Introduced by Assembly Member Corbett**

*(Principal coauthor: Assembly Member Matthews)*

**(Coauthors: Assembly Members Alquist, Aroner, Cardenas, Chan, Chu, Frommer, Keeley, Kehoe, Koretz, Lowenthal, Matthews, Nakano, Pavley, Salinas, Strom-Martin, Thomson, and Wiggins)**

February 23, 2001

---

~~An act to amend Sections 17024.5, 17052.6, 17052.12, 17062, 17063, 17073, 17085, 17140, 17140.3, 17144, 17152, 17279, 17279.4, 17501, 17551, 17570, 17751, 17752, 17760.5, 18521, 19136, 19365, 23038.5, 23051.5, 23456, 23457, 23609, 23701s, 23705, 23711, 23712, 23800.5, 23801, 23802, 23806, 23811, 24273, 24307, 24349, 24355.5, 24357, 24362, 24364, 24369.4, 24407, 24423, 24426, 24651, 24674, 24710, 24872.4, 24944, 24946, and 24949.2 of, to add Sections 17144.5, 17205, 17207.5, 19136.8, and 24347.6 to, and to repeal and add Sections 24377, 24409, 24676, and 24676.5 of, and to repeal Section 18037 of, the Revenue and Taxation Code, relating to taxation, to take effect immediately, tax levy. An act to amend Sections 17024.5,~~

17039, 17052.6, 17052.12, 17062, 17063, 17085, 17140, 17140.3, 17275.5, 17501, 17551, 17560, 17570, 17731.5, 17751, 18038.5, 19136, 19141, 19365, 19521, 23038.5, 23456, 23457, 23609, 23701s, 23705, 23711, 23712, 23801, 23802, 23811, 24357.9, 24424, 24443, 24667, 24710, and 24942 of, to amend and repeal Section 24949.1 of, to add Sections 17062.3, 17132, 17132.6, 17144.5, 17205, 17552.3, 17563.5, 19136.8, 23456.5, 24661.3, and 24685.5 to, and to repeal Sections 17271 and 17279.5 of, the Revenue and Taxation Code, relating to taxation, to take effect immediately, tax levy.

## LEGISLATIVE COUNSEL'S DIGEST

AB 1122, as amended, Corbett. Taxation: federal conformity.

*Under the Personal Income Tax Law and the Bank and Corporation Tax Law, various provisions of the federal Internal Revenue Code, as enacted as of a specified date, are referenced in various sections of the Revenue and Taxation Code. Those laws provide that for taxable years beginning on or after January 1, 1998, the specified date of those referenced Internal Revenue Code sections is January 1, 1998, unless otherwise specifically provided.*

*Existing law requires, for any introduced bill that proposes changes in any of those dates, that the Franchise Tax Board prepare a complete analysis of the bill that describes all changes to state law that will automatically occur by reference to federal law as of the changed date. It further requires the Franchise Tax Board to immediately update and supplement that analysis upon any amendment to the bill, and requires that analysis to be made available to the public and to be submitted to the Legislature for publication in the daily journal of each house of the Legislature.*

*This bill would change the specified date of those referenced Internal Revenue Code sections to January 1, 2001, for taxable years beginning on or after January 1, 2002, and thereby would make numerous substantive changes to both the Personal Income Tax Law and the Bank and Corporation Tax Law with respect to those areas of preexisting conformity that are subject to changes under federal laws enacted after January 1, 1998, and that have not been, or are not being, excepted or modified.*

*This bill would make certain other changes in federal income tax laws applicable, with specified exceptions and modifications, and make specified supplemental, technical, or clarifying changes, for purposes*

*of the Personal Income Tax Law or the Bank and Corporation Tax Law, or both, with respect to, among other things, credits that may reduce certain taxes below the tentative minimum tax, the credit for dependent care expenses, the credit for research and development expenses, adjustments in computing alternative minimum taxable income, the exclusion of extraterritorial income, annuities and certain proceeds of life insurance contracts, the Ricky Ray Hemophilia Relief Fund Act of 1998, the denial of deduction for club dues, the mark to market accounting method, the inapplicability of excise tax on premiums paid, certain amounts paid in connection with insurance contracts, specified federal acts, the installment method of accounting, qualified state tuition programs, the Federal Agriculture Improvement and Reform Act of 1996, determinations relating to deferred compensation, taxation of estates and trusts, small business stock, failure by an individual to pay estimated income tax, underpayment of estimated tax, underpayments of installments, elimination of interest on overlapping periods of tax overpayments and underpayments, mining exploration and development costs, tax-exempt interest, "S corporations," certain publicly traded partnerships treated as corporations, the deduction for a qualified computer contribution, secured indebtedness, tax on passive investment income, securities futures contracts, and the sale or exchange of livestock. This bill would specify various dates on which specified provisions apply, make findings and declarations that certain provisions are declaratory of existing law, and specify the intent and operation in the application of provisions conforming to various federal acts.*

~~Under existing Personal Income Tax Law and the Bank and Corporation Tax Law a taxpayer, generally, has the option to treat specified transactions differently than the manner in which the transaction was elected to be treated for federal income tax purposes.~~

~~This bill would provide, with specified exceptions, that any election made for federal income taxes would apply for state income tax purposes.~~

~~This bill would, for purposes of the Personal Income Tax Law or the Bank and Corporation Tax Law, or both, make certain other changes in conformance with federal law, as specified, with respect to the dependent care expense credit, the treatment of gifts of appreciated property, the penalties imposed for underpayments of estimated taxes, credit for research and development costs, election to treat outdoor advertising displays as real property, filing status, Commodity Credit~~



~~Corporation loans, charitable contribution deduction, amortizable bond premium, certain expenses chargeable to capital account, certain expenditures by farmers, deduction for organizational expenditures of a corporation, intangible drilling and development costs, election to capitalize certain taxes and carrying charges, certain methods of accounting, certain non-interest-bearing and other obligations, prepaid subscription income, magazines, paperbacks, and records returned after the close of the taxable year, the compulsory or involuntary conversion of property, and the election relating to replacement property or stock.~~

The Personal Income Tax Law, in partial conformity with federal law, provides tax benefits for contributions to specified retirement plans.

This bill would, in conformance with the Economic Growth and Tax Relief Reconciliation Act of 2001, expand the tax benefits allowed for contributions to these retirement plans.

This bill would take effect immediately as a tax levy *but would become operative only if SB 657 is chaptered.*

Vote: majority. Appropriation: no. Fiscal committee: yes. State-mandated local program: no.

*The people of the State of California do enact as follows:*

1 ~~SECTION 1. Section 17024.5 of the Revenue and Taxation~~  
2 ~~Code is amended to read:~~

3 ~~17024.5. (a) (1) Unless otherwise specifically provided, the~~  
4 ~~terms "Internal Revenue Code," "Internal Revenue Code of~~  
5 ~~1954," or "Internal Revenue Code of 1986," for purposes of this~~  
6 ~~part, mean Title 26 of the United States Code, including all~~  
7 ~~amendments thereto as enacted on the specified date for the~~  
8 ~~applicable taxable year as follows:~~

9		
10		Specified Date of
11		Internal Revenue
12	Taxable Year	Code Sections
13	(A) For taxable years beginning on or after January 1,	
14	1983, and on or before December 31, 1983 . . .	January 15, 1983
15	(B) For taxable years beginning on or after January 1,	
16	1984, and on or before December 31, 1984 . . .	January 1, 1984
17	(C) For taxable years beginning on or after January 1,	
18	1985, and on or before December 31, 1985 . . .	January 1, 1985

~~(D) For taxable years beginning on or after January 1,~~  
~~1986, and on or before December 31, 1986 . . . .~~ ~~January 1, 1986~~  
~~(E) For taxable years beginning on or after January 1,~~  
~~1987, and on or before December 31, 1988 . . . .~~ ~~January 1, 1987~~  
~~(F) For taxable years beginning on or after January 1,~~  
~~1989, and on or before December 31, 1989 . . . .~~ ~~January 1, 1989~~  
~~(G) For taxable years beginning on or after January 1,~~  
~~1990, and on or before December 31, 1990 . . . .~~ ~~January 1, 1990~~  
~~(H) For taxable years beginning on or after January 1,~~  
~~1991, and on or before December 31, 1991 . . . .~~ ~~January 1, 1991~~  
~~(I) For taxable years beginning on or after January 1,~~  
~~1992, and on or before December 31, 1992 . . . .~~ ~~January 1, 1992~~  
~~(J) For taxable years beginning on or after January 1,~~  
~~1993, and on or before December 31, 1996 . . . .~~ ~~January 1, 1993~~  
~~(K) For taxable years beginning on or after January 1,~~  
~~1997, and on or before December 31, 1997 . . . .~~ ~~January 1, 1997~~  
~~(L) For taxable years beginning on or after~~  
~~January 1, 1998 . . . . .~~ ~~January 1, 1998~~

~~(2) Unless otherwise specifically provided, for federal laws enacted on or after January 1, 1987, and on or before the specified date for the taxable year, uncodified provisions that relate to provisions of the Internal Revenue Code that are incorporated for purposes of this part shall be applicable to the same taxable years as the incorporated provisions.~~

~~(3) Subtitle G (Tax Technical Corrections) and Part I of Subtitle H (Repeal of Expired or Obsolete Provisions) of the Revenue Reconciliation Act of 1990 (Public Law 101-508) modified numerous provisions of the Internal Revenue Code and provisions of prior federal acts, some of which are incorporated by reference into this part. Unless otherwise provided, the provisions described in the preceding sentence, to the extent that they modify provisions that are incorporated into this part, are declaratory of existing law and shall be applied in the same manner and for the same periods as specified in the Revenue Reconciliation Act of 1990.~~

~~(b) Unless otherwise specifically provided, when applying any provision of the Internal Revenue Code for purposes of this part, a reference to any of the following shall not be applicable for purposes of this part:~~

~~(1) Except as provided in Chapter 4.5 (commencing with Section 23800) of Part 11 of Division 2, an electing small business corporation, as defined in Section 1361(b) of the Internal Revenue Code.~~

~~(2) Domestic international sales corporations (DISC), as defined in Section 992(a) of the Internal Revenue Code.~~

~~(3) A personal holding company, as defined in Section 542 of the Internal Revenue Code.~~

~~(4) A foreign personal holding company, as defined in Section 552 of the Internal Revenue Code.~~

~~(5) A foreign investment company, as defined in Section 1246(b) of the Internal Revenue Code.~~

~~(6) A foreign trust, as defined in Section 679 of the Internal Revenue Code.~~

~~(7) Foreign income taxes and foreign income tax credits.~~

~~(8) Section 911 of the Internal Revenue Code, relating to United States citizens living abroad.~~

~~(9) A foreign corporation, except that Section 367 of the Internal Revenue Code shall be applicable.~~

~~(10) Federal tax credits and carryovers of federal tax credits.~~

~~(11) Nonresident aliens.~~

~~(12) Deduction for personal exemptions, as provided in Section 151 of the Internal Revenue Code.~~

~~(13) The tax on generation-skipping transfers imposed by Section 2601 of the Internal Revenue Code.~~

~~(14) The tax, relating to estates, imposed by Section 2001 or 2101 of the Internal Revenue Code.~~

~~(e) (1) The provisions contained in Sections 41 to 44, inclusive, and 172 of the Tax Reform Act of 1984 (Public Law 98-369), relating to treatment of debt instruments, shall not be applicable for taxable years beginning before January 1, 1987.~~

~~(2) The provisions contained in Public Law 99-121, relating to the treatment of debt instruments, shall not be applicable for taxable years beginning before January 1, 1987.~~

~~(3) For each taxable year beginning on or after January 1, 1987, the provisions referred to by paragraphs (1) and (2) shall be applicable for purposes of this part in the same manner and with respect to the same obligations as the federal provisions, except as otherwise provided in this part.~~

1 ~~(d) When applying the Internal Revenue Code for purposes of~~  
2 ~~this part, regulations promulgated in final form or issued as~~  
3 ~~temporary regulations by “the secretary” shall be applicable as~~  
4 ~~regulations under this part to the extent that they do not conflict~~  
5 ~~with this part or with regulations issued by the Franchise Tax~~  
6 ~~Board.~~

7 ~~(e) Whenever this part allows a taxpayer to make an election,~~  
8 ~~on or after January 1, 2002, in taxable years beginning on or after~~  
9 ~~January 1, 2002, the following rules shall apply:~~

10 ~~(1) A proper election for federal income tax purposes filed with~~  
11 ~~the Internal Revenue Service in accordance with the Internal~~  
12 ~~Revenue Code or regulations issued by “the secretary” shall be~~  
13 ~~treated as an election for purposes of this part and a separate~~  
14 ~~election for state purposes shall not be allowed, unless otherwise~~  
15 ~~provided in this part or in regulations issued by the Franchise Tax~~  
16 ~~Board.~~

17 ~~(2) A copy of that election shall be furnished to the Franchise~~  
18 ~~Tax Board upon request.~~

19 ~~(3) If a taxpayer does not make a proper election for federal~~  
20 ~~income tax purposes, a separate election for purposes of this part~~  
21 ~~shall not be allowed unless otherwise provided in this part.~~

22 ~~(f) Whenever this part allows or requires a taxpayer to file an~~  
23 ~~application or seek consent, the rules set forth in subdivision (e)~~  
24 ~~shall be applicable with respect to that application or consent.~~

25 ~~(g) When applying the Internal Revenue Code for purposes of~~  
26 ~~determining the statute of limitations under this part, any reference~~  
27 ~~to a period of three years shall be modified to read four years for~~  
28 ~~purposes of this part.~~

29 ~~(h) When applying, for purposes of this part, any section of the~~  
30 ~~Internal Revenue Code or any applicable regulation thereunder, all~~  
31 ~~of the following shall apply:~~

32 ~~(1) References to “adjusted gross income” shall mean the~~  
33 ~~amount computed in accordance with Section 17072, except as~~  
34 ~~provided in paragraph (2).~~

35 ~~(2) References to “adjusted gross income” for purposes of~~  
36 ~~computing limitations based upon adjusted gross income, shall~~  
37 ~~mean the amount required to be shown as adjusted gross income~~  
38 ~~on the federal tax return for the same taxable year.~~

39 ~~(3) Any reference to “subtitle” or “chapter” shall mean this~~  
40 ~~part.~~



~~(4) The provisions of Section 7806 of the Internal Revenue Code, relating to construction of title, shall apply.~~

~~(5) Any provision of the Internal Revenue Code that becomes operative on or after the specified date for that taxable year shall become operative on the same date for purposes of this part.~~

~~(6) Any provision of the Internal Revenue Code that becomes inoperative on or after the specified date for that taxable year shall become inoperative on the same date for purposes of this part.~~

~~(7) Due account shall be made for differences in federal and state terminology, effective dates, substitution of "Franchise Tax Board" for "secretary" when appropriate, and other obvious differences.~~

~~(i) Any reference to a specific provision of the Internal Revenue Code shall include modifications of that provision, if any, in this part.~~

**SEC. 2.**

*SECTION 1. Section 17024.5 of the Revenue and Taxation Code is amended to read:*

17024.5. (a) (1) Unless otherwise specifically provided, the terms "Internal Revenue Code," "Internal Revenue Code of 1954," or "Internal Revenue Code of 1986," for purposes of this part, mean Title 26 of the United States Code, including all amendments thereto as enacted on the specified date for the applicable taxable year as follows:

Taxable Year	Specified Date of Internal Revenue Code Sections
(A) For taxable years beginning on or after January 1, 1983, and on or before December 31, 1983 . . . .	January 15, 1983
(B) For taxable years beginning on or after January 1, 1984, and on or before December 31, 1984 . . . .	January 1, 1984
(C) For taxable years beginning on or after January 1, 1985, and on or before December 31, 1985 . . . .	January 1, 1985
(D) For taxable years beginning on or after January 1, 1986, and on or before December 31, 1986 . . . .	January 1, 1986
(E) For taxable years beginning on or after January 1, 1987, and on or before December 31, 1988 . . . .	January 1, 1987
(F) For taxable years beginning on or after January 1, 1989, and on or before December 31, 1989 . . . .	January 1, 1989



- 1 (G) For taxable years beginning on or after January 1,
- 2 1990, and on or before December 31, 1990 . . . . January 1, 1990
- 3 (H) For taxable years beginning on or after January 1,
- 4 1991, and on or before December 31, 1991 . . . . January 1, 1991
- 5 (I) For taxable years beginning on or after January 1,
- 6 1992, and on or before December 31, 1992 . . . . January 1, 1992
- 7 (J) For taxable years beginning on or after January 1,
- 8 1993, and on or before December 31, 1996 . . . . January 1, 1993
- 9 (K) For taxable years beginning on or after January 1,
- 10 1997, and on or before December 31, 1997 . . . . January 1, 1997
- 11 (L) For taxable years beginning on or after
- 12 January 1, 1998, *and on or before*
- 13 *December 31, 2001* . . . . . January 1, 1998
- 14 (M) *For taxable years beginning on or after*
- 15 *January 1, 2002* . . . . . *January 1, 2001*

16

17 (2) Unless otherwise specifically provided, for federal laws  
 18 enacted on or after January 1, 1987, and on or before the specified  
 19 date for the taxable year, uncodified provisions that relate to  
 20 provisions of the Internal Revenue Code that are incorporated for  
 21 purposes of this part shall be applicable to the same taxable years  
 22 as the incorporated provisions.

23 (3) Subtitle G (Tax Technical Corrections) and Part I of Subtitle  
 24 H (Repeal of Expired or Obsolete Provisions) of the Revenue  
 25 Reconciliation Act of 1990 (Public Law 101-508) modified  
 26 numerous provisions of the Internal Revenue Code and provisions  
 27 of prior federal acts, some of which are incorporated by reference  
 28 into this part. Unless otherwise provided, the provisions described  
 29 in the preceding sentence, to the extent that they modify provisions  
 30 that are incorporated into this part, are declaratory of existing law  
 31 and shall be applied in the same manner and for the same periods  
 32 as specified in the Revenue Reconciliation Act of 1990.

33 (b) Unless otherwise specifically provided, when applying any  
 34 provision of the Internal Revenue Code for purposes of this part,  
 35 a reference to any of the following shall not be applicable for  
 36 purposes of this part:

- 37 (1) Except as provided in Chapter 4.5 (commencing with
- 38 Section 23800) of Part 11 of Division 2, an electing small business
- 39 corporation, as defined in Section 1361(b) of the Internal Revenue
- 40 Code.

- 1 (2) Domestic international sales corporations (DISC), as  
2 defined in Section 992(a) of the Internal Revenue Code.
- 3 (3) A personal holding company, as defined in Section 542 of  
4 the Internal Revenue Code.
- 5 (4) A foreign personal holding company, as defined in Section  
6 552 of the Internal Revenue Code.
- 7 (5) A foreign investment company, as defined in Section  
8 1246(b) of the Internal Revenue Code.
- 9 (6) A foreign trust, as defined in Section 679 of the Internal  
10 Revenue Code.
- 11 (7) Foreign income taxes and foreign income tax credits.
- 12 (8) Section 911 of the Internal Revenue Code, relating to  
13 United States citizens living abroad.
- 14 (9) A foreign corporation, except that Section 367 of the  
15 Internal Revenue Code shall be applicable.
- 16 (10) Federal tax credits and carryovers of federal tax credits.
- 17 (11) Nonresident aliens.
- 18 (12) Deduction for personal exemptions, as provided in  
19 Section 151 of the Internal Revenue Code.
- 20 (13) The tax on generation-skipping transfers imposed by  
21 Section 2601 of the Internal Revenue Code.
- 22 (14) The tax, relating to estates, imposed by Section 2001 or  
23 2101 of the Internal Revenue Code.
- 24 (c) (1) The provisions contained in Sections 41 to 44,  
25 inclusive, and 172 of the Tax Reform Act of 1984 (Public Law  
26 98-369), relating to treatment of debt instruments, shall not be  
27 applicable for taxable years beginning before January 1, 1987.
- 28 (2) The provisions contained in Public Law 99-121, relating to  
29 the treatment of debt instruments, shall not be applicable for  
30 taxable years beginning before January 1, 1987.
- 31 (3) For each taxable year beginning on or after January 1, 1987,  
32 the provisions referred to by paragraphs (1) and (2) shall be  
33 applicable for purposes of this part in the same manner and with  
34 respect to the same obligations as the federal provisions, except as  
35 otherwise provided in this part.
- 36 (d) When applying the Internal Revenue Code for purposes of  
37 this part, regulations promulgated in final form or issued as  
38 temporary regulations by “the secretary” shall be applicable as  
39 regulations under this part to the extent that they do not conflict

1 with this part or with regulations issued by the Franchise Tax  
2 Board.

3 (e) Whenever this part allows a taxpayer to make an election,  
4 the following rules shall apply:

5 (1) A proper election filed with the Internal Revenue Service  
6 in accordance with the Internal Revenue Code or regulations  
7 issued by “the secretary” shall be deemed to be a proper election  
8 for purposes of this part, unless otherwise provided in this part or  
9 in regulations issued by the Franchise Tax Board.

10 (2) A copy of that election shall be furnished to the Franchise  
11 Tax Board upon request.

12 (3) To obtain treatment other than that elected for federal  
13 purposes, a separate election shall be filed at the time and in the  
14 manner required by the Franchise Tax Board.

15 (f) Whenever this part allows or requires a taxpayer to file an  
16 application or seek consent, the rules set forth in subdivision (e)  
17 shall be applicable with respect to that application or consent.

18 (g) When applying the Internal Revenue Code for purposes of  
19 determining the statute of limitations under this part, any reference  
20 to a period of three years shall be modified to read four years for  
21 purposes of this part.

22 (h) When applying, for purposes of this part, any section of the  
23 Internal Revenue Code or any applicable regulation thereunder, all  
24 of the following shall apply:

25 (1) References to “adjusted gross income” shall mean the  
26 amount computed in accordance with Section 17072, except as  
27 provided in paragraph (2).

28 (2) References to “adjusted gross income” for purposes of  
29 computing limitations based upon adjusted gross income, shall  
30 mean the amount required to be shown as adjusted gross income  
31 on the federal tax return for the same taxable year.

32 (3) Any reference to “subtitle” or “chapter” shall mean this  
33 part.

34 (4) The provisions of Section 7806 of the Internal Revenue  
35 Code, relating to construction of title, shall apply.

36 (5) Any provision of the Internal Revenue Code that becomes  
37 operative on or after the specified date for that taxable year shall  
38 become operative on the same date for purposes of this part.

(6) Any provision of the Internal Revenue Code that becomes inoperative on or after the specified date for that taxable year shall become inoperative on the same date for purposes of this part.

(7) Due account shall be made for differences in federal and state terminology, effective dates, substitution of “Franchise Tax Board” for “secretary” when appropriate, and other obvious differences.

(i) Any reference to a specific provision of the Internal Revenue Code shall include modifications of that provision, if any, in this part.

*SEC. 2. Section 17039 of the Revenue and Taxation Code is amended to read:*

17039. (a) Notwithstanding any provision in this part to the contrary, for the purposes of computing tax credits, the term “net tax” means the tax imposed under either Section 17041 or 17048 plus the tax imposed under Section 17504 (relating to lump-sum distributions) less the credits allowed by Section 17054 (relating to personal exemption credits) and any amount imposed under paragraph (1) of subdivision (d) and paragraph (1) of subdivision (e) of Section 17560. Notwithstanding the preceding sentence, the “net tax” shall not be less than the tax imposed under Section 17504 (relating to the separate tax on lump-sum distributions), if any. Credits shall be allowed against “net tax” in the following order:

(1) Credits that do not contain carryover or refundable provisions, except those described in paragraphs (4) and (5).

(2) Credits that contain carryover provisions but do not contain refundable provisions.

(3) Credits that contain both carryover and refundable provisions.

(4) The minimum tax credit allowed by Section 17063 (relating to the alternative minimum tax).

(5) Credits for taxes paid to other states allowed by Chapter 12 (commencing with Section 18001).

(6) Credits that contain refundable provisions but do not contain carryover provisions.

The order within each paragraph shall be determined by the Franchise Tax Board.

(b) Notwithstanding the provisions of Sections 17061 (relating to refunds pursuant to the Unemployment Insurance Code) and

1 19002 (relating to tax withholding), the credits provided in those  
2 sections shall be allowed in the order provided in paragraph (6) of  
3 subdivision (a).

4 (c) (1) Notwithstanding any other provision of this part, no tax  
5 credit shall reduce the tax imposed under Section 17041 or 17048  
6 plus the tax imposed under Section 17504 (relating to the separate  
7 tax on lump-sum distributions) below the tentative minimum tax,  
8 as defined by Section 17062, except the following credits, but only  
9 after allowance of the credit allowed by Section 17063:

10 (A) The credit allowed by Section 17052.2 (relating to teacher  
11 retention tax credit).

12 (B) The credit allowed by former Section 17052.4 (relating to  
13 solar energy).

14 (C) The credit allowed by former Section 17052.5 (relating to  
15 solar-energy energy, repealed on January 1, 1987).

16 (D) The credit allowed by former Section 17052.5 (relating to  
17 solar-energy energy, repealed on December 1, 1994).

18 (E) The credit allowed by Section 17052.12 (relating to  
19 research expenses).

20 (F) The credit allowed by former Section 17052.13 (relating to  
21 sales and use tax credit).

22 (G) The credit allowed by former Section 17052.15 (relating to  
23 Los Angeles Revitalization Zone sales tax credit).

24 (H) *The credit allowed by Section 17052.25 (relating to*  
25 *adoption costs credit).*

26 (I) The credit allowed by Section 17053.5 (relating to the  
27 renter's credit).

28 ~~(I)~~

29 (J) The credit allowed by former Section 17053.8 (relating to  
30 enterprise zone hiring credit).

31 ~~(J)~~

32 (K) The credit allowed by former Section 17053.10 (relating to  
33 Los Angeles Revitalization Zone hiring credit).

34 ~~(K)~~

35 (L) The credit allowed by former Section 17053.11 (relating to  
36 program area hiring credit).

37 ~~(L)~~

38 (M) For each taxable year beginning on or after January 1,  
39 1994, the credit allowed by former Section 17053.17 (relating to  
40 Los Angeles Revitalization Zone hiring credit).

- 1     ~~(M)~~—  
2     (N) The credit allowed by Section 17053.33 (relating to  
3 targeted tax area sales or use tax credit).  
4     ~~(N)~~—  
5     (O) The credit allowed by Section 17053.34 (relating to  
6 targeted tax area hiring credit).  
7     ~~(O)~~—  
8     (P) The credit allowed by Section 17053.49 (relating to  
9 qualified property).  
10    ~~(P)~~—  
11    (Q) The credit allowed by Section 17053.70 (relating to  
12 enterprise zone sales or use tax credit).  
13    ~~(Q)~~—  
14    (R) The credit allowed by Section 17053.74 (relating to  
15 enterprise zone hiring credit).  
16    ~~(R)~~—  
17    (S) The credit allowed by Section 17054 (relating to credits for  
18 personal exemption).  
19    ~~(S)~~—  
20    (T) *The credit allowed by Section 17054.5 (relating to credits*  
21 *for qualified joint custody head of household and qualified*  
22 *taxpayer with a dependent parent).*  
23    (U) *The credit allowed by Section 17054.7 (relating to*  
24 *qualified senior head of household credit).*  
25    (V) The credit allowed by *former* Section 17057 (relating to  
26 clinical testing expenses).  
27    ~~(T)~~—  
28    (W) The credit allowed by Section 17058 (relating to  
29 low-income housing).  
30    ~~(U)~~—  
31    (X) The credit allowed by Section 17061 (relating to refunds  
32 pursuant to the Unemployment Insurance Code).  
33    ~~(V)~~—  
34    (Y) Credits for taxes paid to other states allowed by Chapter 12  
35 (commencing with Section 18001).  
36    ~~(W)~~—  
37    (Z) The credit allowed by Section 19002 (relating to tax  
38 withholding).  
39    (2) Any credit that is partially or totally denied under paragraph  
40 (1) shall be allowed to be carried over and applied to the net tax in



1 succeeding taxable years, if the provisions relating to that credit  
2 include a provision to allow a carryover when that credit exceeds  
3 the net tax.

4 (d) Unless otherwise provided, any remaining carryover of a  
5 credit allowed by a section that has been repealed or made  
6 inoperative shall continue to be allowed to be carried over under  
7 the provisions of that section as it read immediately prior to being  
8 repealed or becoming inoperative.

9 (e) (1) Unless otherwise provided, if two or more taxpayers  
10 (other than husband and wife) share in costs that would be eligible  
11 for a tax credit allowed under this part, each taxpayer shall be  
12 eligible to receive the tax credit in proportion to his or her  
13 respective share of the costs paid or incurred.

14 (2) In the case of a partnership, the credit shall be allocated  
15 among the partners pursuant to a written partnership agreement in  
16 accordance with Section 704 of the Internal Revenue Code,  
17 relating to partner's distributive share.

18 (3) In the case of a husband and wife who file separate returns,  
19 the credit may be taken by either or equally divided between them.

20 (f) Unless otherwise provided, in the case of a partnership, any  
21 credit allowed by this part shall be computed at the partnership  
22 level, and any limitation on the expenses qualifying for the credit  
23 or limitation upon the amount of the credit shall be applied to the  
24 partnership and to each partner.

25 (g) (1) With respect to any taxpayer that directly or indirectly  
26 owns an interest in a business entity that is disregarded for tax  
27 purposes pursuant to Section 23038 and any regulations  
28 thereunder, the amount of any credit or credit carryforward  
29 allowable for any taxable year attributable to the disregarded  
30 business entity shall be limited in accordance with paragraphs (2)  
31 and (3).

32 (2) The amount of any credit otherwise allowed under this part,  
33 including any credit carryover from prior years, that may be  
34 applied to reduce the taxpayer's "net tax," as defined in  
35 subdivision (a), for the taxable year shall be limited to an amount  
36 equal to the excess of the taxpayer's regular tax (as defined in  
37 Section 17062), determined by including income attributable to  
38 the disregarded business entity that generated the credit or credit  
39 carryover, over the taxpayer's regular tax (as defined in Section  
40 17062), determined by excluding the income attributable to that



disregarded business entity. No credit shall be allowed if the taxpayer's regular tax (as defined in Section 17062), determined by including the income attributable to the disregarded business entity, is less than the taxpayer's regular tax (as defined in Section 17062), determined by excluding the income attributable to the disregarded business entity.

(3) If the amount of a credit allowed pursuant to the section establishing the credit exceeds the amount allowable under this subdivision in any taxable year, the excess amount may be carried over to subsequent taxable years pursuant to subdivisions (c) and (d).

*SEC. 3.* Section 17052.6 of the Revenue and Taxation Code is amended to read:

17052.6. (a) For each taxable year beginning on or after January 1, 2000, there shall be allowed as a credit against the "net tax" (as defined in Section 17039) an amount determined in accordance with Section 21 of the Internal Revenue Code, as modified by the Economic Growth and Tax Relief Reconciliation Act of 2001 (Public Law 107-16), except that the amount of the credit shall be a percentage, as provided in subdivision (b) of the allowable federal credit without taking into account whether there is a federal tax liability.

(b) For the purposes of subdivision (a), the percentage of the allowable federal credit shall be determined as follows:

If the California adjusted gross income is:	The percentage of credit is:
\$40,000 or less . . . . .	63%
Over \$40,000 but not over \$70,000 . . . . .	53%
Over \$70,000 but not over \$100,000 . . . . .	42%
Over \$100,000 . . . . .	0%

(c) In the case of a taxpayer whose credits provided under this section exceed the taxpayer's tax liability computed under this part, the excess shall be credited against other amounts due, if any, from the taxpayer and the balance, if any, shall be paid from the Tax Relief and Refund Account and refunded to the taxpayer.

(d) For purposes of this section, California adjusted gross income means California adjusted gross income as computed for purposes of Section 17041.

(e) The credit authorized by this section shall be limited to those taxpayers who, during the taxable year, maintain a household, within the meaning of Section 21(e)(1) of the Internal Revenue Code, that is located within this state.

~~SEC. 2.5. Section 17052.12 of the Revenue and Taxation Code is amended to read:~~

~~17052.12. For each taxable year beginning on or after January 1, 1987, there shall be allowed as a credit against the "net tax" (as defined by Section 17039) for the taxable year an amount determined in accordance with Section 41 of the Internal Revenue Code, except as follows:~~

~~(a) For each taxable year beginning before January 1, 1997, the reference to "20 percent" in Section 41(a)(1) of the Internal Revenue Code is modified to read "8 percent."~~

~~(b) (1) For each taxable year beginning on or after January 1, 1997, and before January 1, 1999, the reference to "20 percent" in Section 41(a)(1) of the Internal Revenue Code is modified to read "11 percent."~~

~~(2) For each taxable year beginning on or after January 1, 1999, and before January 1, 2000, the reference to "20 percent" in Section 41(a)(1) of the Internal Revenue Code is modified to read "12 percent."~~

~~(3) For each taxable year beginning on or after January 1, 2000, the reference to "20 percent" in Section 41(a)(1) of the Internal Revenue Code is modified to read "15 percent."~~

~~(c) Section 41(a)(2) of the Internal Revenue Code, relating to basic research payments, shall not apply.~~

~~(d) "Qualified research" shall include only research conducted in California.~~

~~(e) In the case where the credit allowed under this section exceeds the "net tax," the excess may be carried over to reduce the "net tax" in the following year, and succeeding years if necessary, until the credit has been exhausted.~~

~~(f) (1) With respect to any expense paid or incurred after the operative date of Section 6378, Section 41(b)(1) of the Internal Revenue Code is modified to exclude from the definition of "qualified research expense" any amount paid or incurred for tangible personal property that is eligible for the exemption from sales or use tax provided by Section 6378.~~

~~(2) For each taxable year beginning on or after January 1, 1998, the reference to “Section 501(a)” in Section 41(b)(3)(C) of the Internal Revenue Code, relating to contract research expenses, is modified to read “this part or Part 11 (commencing with Section 23001).”~~

~~(g) (1) For each taxable year beginning on or after January 1, 1998, and before January 1, 2000:~~

~~(A) The reference to “1.65 percent” in Section 41(e)(4)(A)(i) of the Internal Revenue Code is modified to read “one and thirty-two hundredths of one percent.”~~

~~(B) The reference to “2.2 percent” in Section 41(e)(4)(A)(ii) of the Internal Revenue Code is modified to read “one and seventy-six hundredths of one percent.”~~

~~(C) The reference to “2.75 percent” in Section 41(e)(4)(A)(iii) of the Internal Revenue Code is modified to read “two and two-tenths of one percent.”~~

~~(2) For each taxable year beginning on or after January 1, 2000:~~

~~(A) The reference to “1.65 percent” in Section 41(e)(4)(A)(i) of the Internal Revenue Code is modified to read “one and forty-nine hundredths of one percent.”~~

~~(B) The reference to “2.2 percent” in Section 41(e)(4)(A)(ii) of the Internal Revenue Code is modified to read “one and ninety-eight hundredths of one percent.”~~

~~(C) The reference to “2.75 percent” in Section 41(e)(4)(A)(iii) of the Internal Revenue Code is modified to read “two and forty-eight hundredths of one percent.”~~

~~(3) Section 41(e)(6) of the Internal Revenue Code, relating to gross receipts, is modified to take into account only those gross receipts from the sale of property held primarily for sale to customers in the ordinary course of the taxpayer’s trade or business that is delivered or shipped to a purchaser within this state, regardless of f.o.b. point or any other condition of the sale.~~

~~(h) Section 41(h) of the Internal Revenue Code, relating to termination, shall not apply.~~

~~(i) Section 41(g) of the Internal Revenue Code, relating to special rule for passthrough of credit, is modified by each of the following:~~

~~(1) The last sentence shall not apply.~~

~~(2) If the amount determined under Section 41(a) of the Internal Revenue Code for any taxable year exceeds the limitation~~

1 of Section 41(g) of the Internal Revenue Code, that amount may  
2 be carried over to other taxable years under the rules of subdivision  
3 (e); except that the limitation of Section 41(g) of the Internal  
4 Revenue Code shall be taken into account in each subsequent  
5 taxable year.

6 ~~SEC. 3.—~~

7 *SEC. 4. Section 17052.12 of the Revenue and Taxation Code*  
8 *is amended to read:*

9 17052.12. For each taxable year beginning on or after January  
10 1, 1987, there shall be allowed as a credit against the “net tax” (as  
11 defined by Section 17039) for the taxable year an amount  
12 determined in accordance with Section 41 of the Internal Revenue  
13 Code, except as follows:

14 (a) For each taxable year beginning before January 1, 1997, the  
15 reference to “20 percent” in Section 41(a)(1) of the Internal  
16 Revenue Code is modified to read “8 percent.”

17 (b) (1) For each taxable year beginning on or after January 1,  
18 1997, and before January 1, 1999, the reference to “20 percent”  
19 in Section 41(a)(1) of the Internal Revenue Code is modified to  
20 read “11 percent.”

21 (2) For each taxable year beginning on or after January 1, 1999,  
22 and before January 1, 2000, the reference to “20 percent” in  
23 Section 41(a)(1) of the Internal Revenue Code is modified to read  
24 “12 percent.”

25 (3) For each taxable year beginning on or after January 1, 2000,  
26 the reference to “20 percent” in Section 41(a)(1) of the Internal  
27 Revenue Code is modified to read “15 percent.”

28 (c) Section 41(a)(2) of the Internal Revenue Code, relating to  
29 basic research payments, shall not apply.

30 (d) “Qualified research” shall include only research conducted  
31 in California.

32 (e) In the case where the credit allowed under this section  
33 exceeds the “net tax,” the excess may be carried over to reduce the  
34 “net tax” in the following year, and succeeding years if necessary,  
35 until the credit has been exhausted.

36 (f) (1) With respect to any expense paid or incurred after the  
37 operative date of Section 6378, Section 41(b)(1) of the Internal  
38 Revenue Code is modified to exclude from the definition of  
39 “qualified research expense” any amount paid or incurred for

1 tangible personal property that is eligible for the exemption from  
2 sales or use tax provided by Section 6378.

3 (2) For each taxable year beginning on or after January 1, 1998,  
4 the reference to “Section 501(a)” in Section 41(b)(3)(C) of the  
5 Internal Revenue Code, relating to contract research expenses, is  
6 modified to read “this part or Part 11 (commencing with Section  
7 23001).”

8 ~~(g) (1) For each taxable year beginning on or after January 1,~~  
9 ~~1998, and before January 1, 2000:~~

10 ~~(A) The reference to “1.65 percent” in Section 41(c)(4)(A)(i)~~  
11 ~~of the Internal Revenue Code is modified to read “one and~~  
12 ~~thirty-two hundredths of one percent.”~~

13 ~~(B) The reference to “2.2 percent” in Section 41(c)(4)(A)(ii)~~  
14 ~~of the Internal Revenue Code is modified to read “one and~~  
15 ~~seventy-six hundredths of one percent.”~~

16 ~~(C) The reference to “2.75 percent” in Section 41(c)(4)(A)(iii)~~  
17 ~~of the Internal Revenue Code is modified to read “two and~~  
18 ~~two-tenths of one percent.”~~

19 ~~(2) For each taxable year beginning on or after January 1, 2000:~~

20 (A) The reference to ~~“1.65~~ “2.65 percent” in Section  
21 41(c)(4)(A)(i) of the Internal Revenue Code is modified to read  
22 “one and forty-nine hundredths of one percent.”

23 (B) The reference to ~~“2.2~~ “3.2 percent” in Section  
24 41(c)(4)(A)(ii) of the Internal Revenue Code is modified to read  
25 “one and ninety-eight hundredths of one percent.”

26 (C) The reference to ~~“2.75~~ “3.75 percent” in Section  
27 41(c)(4)(A)(iii) of the Internal Revenue Code is modified to read  
28 “two and forty-eight hundredths of one percent.”

29 ~~(3)–~~

30 (2) Section 41(c)(4)(B) shall not apply and in lieu thereof an  
31 election under Section 41(c)(4)(A) of the Internal Revenue Code  
32 may be made for any taxable year of the taxpayer beginning on or  
33 after January 1, 1998. That election shall apply to the taxable year  
34 for which made and all succeeding taxable years unless revoked  
35 with the consent of the Franchise Tax Board.

36 ~~(4)–~~

37 (3) Section 41(c)(6) of the Internal Revenue Code, relating to  
38 gross receipts, is modified to take into account only those gross  
39 receipts from the sale of property held primarily for sale to  
40 customers in the ordinary course of the taxpayer’s trade or business

1 that is delivered or shipped to a purchaser within this state,  
2 regardless of f.o.b. point or any other condition of the sale.

3 (h) Section 41(h) of the Internal Revenue Code, relating to  
4 termination, shall not apply.

5 (i) Section 41(g) of the Internal Revenue Code, relating to  
6 special rule for passthrough of credit, is modified by each of the  
7 following:

8 (1) The last sentence shall not apply.

9 (2) If the amount determined under Section 41(a) of the  
10 Internal Revenue Code for any taxable year exceeds the limitation  
11 of Section 41(g) of the Internal Revenue Code, that amount may  
12 be carried over to other taxable years under the rules of subdivision  
13 (e); except that the limitation of Section 41(g) of the Internal  
14 Revenue Code shall be taken into account in each subsequent  
15 taxable year.

16 *SEC. 5.* Section 17062 of the Revenue and Taxation Code is  
17 amended to read:

18 17062. (a) In addition to the other taxes imposed by this part,  
19 there is hereby imposed for each taxable year, a tax equal to the  
20 excess, if any, of—

21 (1) The tentative minimum tax for the taxable year, over

22 (2) The regular tax for the taxable year.

23 (b) For purposes of this chapter, each of the following shall  
24 apply:

25 (1) The tentative minimum tax shall be computed in  
26 accordance with Sections 55 to 59, inclusive, of the Internal  
27 Revenue Code, except as otherwise provided in this part.

28 (2) The regular tax shall be the amount of tax imposed by  
29 Section 17041 or 17048, before reduction for any credits against  
30 the tax, less any amount imposed under paragraph (1) of  
31 subdivision (d) and paragraph (1) of subdivision (e) of Section  
32 17560.

33 (3) (A) The provisions of Section 55(b)(1) of the Internal  
34 Revenue Code shall be modified to provide that the tentative  
35 minimum tax for the taxable year shall be equal to the following  
36 percent of so much of the alternative minimum taxable income for  
37 the taxable year as exceeds the exemption amount, before  
38 reduction for any credits against the tax:

39 (i) For any taxable year beginning on or after January 1, 1991,  
40 and before January 1, 1996, 8.5 percent.

1 (ii) For any taxable year beginning on or after January 1, 1996,  
2 7 percent.

3 (B) In the case of a nonresident or part-year resident, the  
4 tentative minimum tax shall be computed by multiplying the  
5 alternative minimum taxable income of the nonresident or  
6 part-year resident, as defined in subparagraph (C), by a rate  
7 (expressed as a percentage) equal to the tax computed under  
8 subdivision (b) on the alternative minimum taxable income of the  
9 nonresident or part-year resident as if the nonresident or part-year  
10 resident were a resident of this state for the taxable year and as if  
11 the nonresident or part-year resident were a resident of this state  
12 for all prior taxable years for any carryover items, deferred  
13 income, suspended losses, or suspended deductions, divided by  
14 the amount of that income.

15 (C) For purposes of this section, the term “alternative  
16 minimum taxable income of a nonresident or part-year resident”  
17 includes each of the following:

18 (i) For any period during which the taxpayer was a resident of  
19 this state (as defined by Section 17014), all items of alternative  
20 minimum taxable income (as modified for purposes of this  
21 chapter), regardless of source.

22 (ii) For any period during which the taxpayer was not a resident  
23 of this state, alternative minimum taxable income (as modified for  
24 purposes of this chapter) which were derived from sources within  
25 this state, determined in accordance with Article 9 of Chapter 3  
26 (commencing with Section 17301) and Chapter 11 (commencing  
27 with Section 17951).

28 (iii) For purposes of computing “alternative minimum taxable  
29 income of a nonresident or part-year resident,” any carryover  
30 items, deferred income, suspended losses, or suspended  
31 deductions shall only be allowable to the extent that the carryover  
32 item, suspended loss, or suspended deduction was derived from  
33 sources within this state.

34 (4) The provisions of Section 55(b)(2) of the Internal Revenue  
35 Code, relating to alternative minimum taxable income, shall be  
36 modified to provide that alternative minimum taxable income  
37 shall not include the income, adjustments, and items of tax  
38 preference attributable to any trade or business of a qualified  
39 taxpayer.



1 (A) For purposes of this paragraph, “qualified taxpayer”  
2 means a taxpayer who meets both of the following:

3 (i) Is the owner of, or has an ownership interest in, a trade or  
4 business.

5 (ii) Has aggregate gross receipts, less returns and allowances,  
6 of less than one million dollars (\$1,000,000) during the taxable  
7 year from all trades or businesses of which the taxpayer is the  
8 owner or has an ownership interest, in the amount of that  
9 taxpayer’s proportionate interest in each trade or business.

10 (B) For purposes of this paragraph, “aggregate gross receipts,  
11 less returns and allowances” means the sum of the gross receipts  
12 of the trades or businesses which the taxpayer owns and the  
13 proportionate interest of the gross receipts of the trades or  
14 businesses which the taxpayer owns and of pass-through entities  
15 in which the taxpayer holds an interest.

16 (C) For purposes of this paragraph, “gross receipts, less returns  
17 and allowances” means the sum of the gross receipts from the  
18 production of business income, as defined in subdivision (a) of  
19 Section 25120, and the gross receipts from the production of  
20 nonbusiness income, as defined in subdivision (d) of Section  
21 25120.

22 (D) For purposes of this paragraph, “proportionate interest”  
23 means:

24 (i) In the case of a pass-through entity which reports a profit for  
25 the taxable year, the taxpayer’s profit interest in the entity at the  
26 end of the taxpayer’s taxable year.

27 (ii) In the case of a pass-through entity which reports a loss for  
28 the taxable year, the taxpayer’s loss interest in the entity at the end  
29 of the taxpayer’s taxable year.

30 (iii) In the case of a pass-through entity which is sold or  
31 liquidates during the taxable year, the taxpayer’s capital account  
32 interest in the entity at the time of the sale or liquidation.

33 (E) (i) For purposes of this paragraph, “proportionate  
34 interest” includes an interest in a pass-through entity.

35 (ii) For purposes of this paragraph, “pass-through entity”  
36 means any of the following:

37 (I) A partnership, as defined by Section 17008.

38 (II) An S corporation, as provided in Chapter 4.5 (commencing  
39 with Section 23800) of Part 11.

1 (III) A regulated investment company, as provided in Section  
2 24871.

3 (IV) A real estate investment trust, as provided in Section  
4 24872.

5 (V) A real estate mortgage investment conduit, as provided in  
6 Section 24874.

7 (5) For taxable years beginning on or after January 1, 1998,  
8 Section 55(d)(1) of the Internal Revenue Code, relating to  
9 exemption amount for taxpayers other than corporations is  
10 modified, for purposes of this part, to provide the following  
11 exemption amounts in lieu of those contained therein:

12 (A) Fifty-seven thousand two hundred sixty dollars (\$57,260)  
13 in the case of either of the following:

14 (i) A joint return.

15 (ii) A surviving spouse.

16 (B) Forty-two thousand nine hundred forty-five dollars  
17 (\$42,945) in the case of an individual who is both of the following:

18 (i) Not a married individual.

19 (ii) Not a surviving spouse.

20 (C) Twenty-eight thousand six hundred thirty dollars  
21 (\$28,630) in the case of either of the following:

22 (i) A married individual who files a separate return.

23 (ii) An estate or trust.

24 (6) For taxable years beginning on or after January 1, 1998,  
25 Section 55(d)(3) of the Internal Revenue Code, relating to the  
26 phaseout of exemption amount for taxpayers other than  
27 corporations is modified, for purposes of this part, to provide the  
28 following phaseout of exemption amounts in lieu of those  
29 contained therein:

30 (A) Two hundred fourteen thousand seven hundred  
31 twenty-five dollars (\$214,725) in the case of a taxpayer described  
32 in subparagraph (A) of paragraph (5).

33 (B) One hundred sixty-one thousand forty-four dollars  
34 (\$161,044) in the case of a taxpayer described in subparagraph (B)  
35 of paragraph (5).

36 (C) One hundred seven thousand three hundred sixty-two  
37 dollars (\$107,362) in the case of a taxpayer described in  
38 subparagraph (C) of paragraph (5).

39 (7) For each taxable year beginning on or after January 1, 1999,  
40 the Franchise Tax Board shall recompute the exemption amounts

prescribed in paragraph (5) and the phaseout of exemption amounts prescribed in paragraph (6). Those computations shall be made as follows:

(A) The California Department of Industrial Relations shall transmit annually to the Franchise Tax Board the percentage change in the California Consumer Price Index for all items from June of the prior calendar year to June of the current calendar year, no later than August 1 of the current calendar year.

(B) The Franchise Tax Board shall do both of the following:

(i) Compute an inflation adjustment factor by adding 100 percent to the percentage change figure that is furnished pursuant to subparagraph (A) and dividing the result by 100.

(ii) Multiply the preceding taxable year exemption amounts and the phaseout of exemption amounts by the inflation adjustment factor determined in clause (i) and round off the resulting products to the nearest one dollar (\$1).

(c) (1) (A) Section 56(a)(6) of the Internal Revenue Code as in effect on January 1, 1997, relating to installment sales of certain property, shall not apply to payments received in taxable years beginning on or after January 1, 1997, with respect to dispositions occurring in taxable years beginning after December 31, 1987.

(B) This paragraph shall not apply to taxable years beginning on or after January 1, 1998.

(2) Section 56(b)(1)(E) of the Internal Revenue Code, relating to standard deduction and deduction for personal exemptions not allowed, is modified, for purposes of this part, to deny the standard deduction allowed by Section 17073.5.

(3) Section 56(b)(3) of the Internal Revenue Code, relating to treatment of incentive stock options, shall be modified to additionally provide the following:

(A) Section 421 of the Internal Revenue Code shall not apply to the transfer of stock acquired pursuant to the exercise of a California qualified stock option under Section 17502.

(B) Section 422(c)(2) of the Internal Revenue Code shall apply in any case where the disposition and inclusion of a California qualified stock option for purposes of this chapter are within the same taxable year and that section shall not apply in any other case.

(C) The adjusted basis of any stock acquired by the exercise of a California qualified stock option shall be determined on the basis of the treatment prescribed by this paragraph.

(d) The provisions of Section 57(a)(5) of the Internal Revenue Code, relating to tax-exempt interest shall not apply.

(e) Section 57(a) of the Internal Revenue Code, relating to items of tax preference, is modified to include as an item of tax preference an amount equal to one-half of the amount excluded from gross income for the taxable year under Section 18152.5.

(f) The provisions of Section 59(a) of the Internal Revenue Code, relating to the alternative minimum tax foreign tax credit, shall not apply.

~~SEC. 4.—~~

*SEC. 6. Section 17062.3 is added to the Revenue and Taxation Code, to read:*

*17062.3. The amendments made to Section 56, relating to adjustments in computing alternative minimum taxable income, by Section 4(1) of Public Law 106-519, relating to the exclusion under Section 114 of the Internal Revenue Code, shall not apply.*

*SEC. 7. Section 17063 of the Revenue and Taxation Code is amended to read:*

17063. (a) There shall be allowed as a credit against the net tax (as defined by Section 17039) for any taxable year an amount equal to the minimum tax credit for that taxable year.

(b) For purposes of subdivision (a), the minimum tax credit shall be determined in accordance with Section 53 of the Internal Revenue Code, except as otherwise provided in this part.

(c) For purposes of this chapter, the amount determined under Section 53(c)(1) of the Internal Revenue Code shall be the regular tax as defined by paragraph (2) of subdivision (b) of Section 17062, reduced by the sum of the credits allowable under this part, other than:

(1) The credits described in paragraph (7) of subdivision (a) of Section 17039.

(2) Any credit which reduces the tax below the tentative minimum tax, as defined by Section 17062.

(d) Section 53(d)(1)(B)(ii)(II) of the Internal Revenue Code, relating to credit not allowed for exclusion preferences, is modified to include subdivision (e) of Section 17062, as a specified item.

~~SEC. 5.—Section 17073 of the Revenue and Taxation Code is amended to read:~~

1 ~~17073. (a) Section 63 of the Internal Revenue Code, relating~~  
2 ~~to taxable income defined, shall apply, except as otherwise~~  
3 ~~provided.~~

4 ~~(b) Notwithstanding subdivision (e) of Section 17024.5, an~~  
5 ~~individual may make a separate state election to itemize~~  
6 ~~deductions under Section 63(c) of the Internal Revenue Code.~~

7 ~~(c) The deduction allowed by Section 17208.1, relating to~~  
8 ~~interest on loans or financed indebtedness obtained from a publicly~~  
9 ~~owned utility for the purchase and installation of energy efficient~~  
10 ~~products or equipment, shall not be treated as a miscellaneous~~  
11 ~~itemized deduction under Section 67(a) of the Internal Revenue~~  
12 ~~Code, relating to the 2-percent floor on miscellaneous deductions.~~

13 ~~(d) For individuals who do not itemize deductions, the standard~~  
14 ~~deduction computed in accordance with Section 17073.5 shall be~~  
15 ~~allowed as a deduction in computing taxable income.~~

16 ~~SEC. 6.—~~

17 *SEC. 8.* Section 17085 of the Revenue and Taxation Code is  
18 amended to read:

19 17085. Section 72 of the Internal Revenue Code, as amended  
20 by the Economic Growth and Tax Relief Reconciliation Act of  
21 2001 (Public Law 107-16), relating to annuities and certain  
22 proceeds of life insurance contracts, is modified as follows:

23 (a) The amendments and transitional rules made by Public Law  
24 99-514 shall be applicable to this part for the same transactions and  
25 the same years as they are applicable for federal income tax  
26 purposes, except that the repeal of Section 72(d) of the Internal  
27 Revenue Code, relating to repeal of special rule for employees'  
28 annuities, shall apply only to the following:

29 (1) Any individual whose annuity starting date is after  
30 December 31, 1986.

31 (2) At the election of the taxpayer, any individual whose  
32 annuity starting date is after July 1, 1986, and before January 1,  
33 1987.

34 (b) The amount of a distribution from an individual retirement  
35 account or annuity or employees' trust or employee annuity that  
36 is includable in gross income for federal income tax purposes shall  
37 be reduced for purposes of this part by the lesser of either of the  
38 following:

39 (1) An amount equal to the amount includable in federal gross  
40 income for the taxable year.

(2) An amount equal to the basis in the account or annuity allowed by Section 17507 (relating to individual retirement accounts and simplified employee pensions) or the increased basis allowed by Sections 17504 and 17506 (relating to plans of self-employed individuals), the increased basis allowed by Section 17501, or the increased basis allowed by Section 17551 that is remaining after adjustment for reductions in gross income under this provision in prior taxable years.

(c) (1) Except as provided in paragraph (2), the amount of the penalty imposed under this part shall be computed in accordance with Sections 72(m), (q), (t), and (v) of the Internal Revenue Code using a rate of  $2\frac{1}{2}$  percent, in lieu of the rate provided in those sections.

(2) In the case where Section 72(t)(6) of the Internal Revenue Code, relating to special rules for simple retirement accounts, applies, the rate in paragraph (1) shall be 6 percent in lieu of the  $2\frac{1}{2}$  percent rate specified therein.

(d) Section 72(f)(2) of the Internal Revenue Code, relating to special rules for computing employees' contributions, shall be applicable without applying the exceptions which immediately follow that paragraph.

~~SEC. 7.—~~

*SEC. 9. Section 17132 is added to the Revenue and Taxation Code, to read:*

*17132. Section 114 of the Internal Revenue Code, relating to extraterritorial income, shall not apply.*

*SEC. 10. Section 17132.6 is added to the Revenue and Taxation Code, to read:*

*17132.6. A payment under Section 103(c)(1) of the Ricky Ray Hemophilia Relief Fund Act of 1998 (Public Law 105-369) to an individual shall be treated for purposes of this part, Part 10.2 (commencing with Section 18401), and Part 11 (commencing with Section 23001) as damages described in Section 104(a)(2) of the Internal Revenue Code.*

*SEC. 11. Section 17140 of the Revenue and Taxation Code is amended to read:*

*17140. (a) For purposes of this section, the following terms have the following meanings as provided in the Golden State Scholarshare Trust Act (Article 19 (commencing with Section 69980) of Chapter 2 of Part 42 of the Education Code):*

1 (1) “Beneficiary” has the meaning set forth in subdivision (c)  
2 of Section 69980 of the Education Code.

3 (2) “Benefit” has the meaning set forth in subdivision (d) of  
4 Section 69980 of the Education Code.

5 (3) “Participant” has the meaning set forth in subdivision (h)  
6 of Section 69980 of the Education Code.

7 (4) “Participation agreement” has the meaning set forth in  
8 subdivision (i) of Section 69980 of the Education Code.

9 (5) “Scholarshare trust” has the meaning set forth in  
10 subdivision (f) of Section 69980 of the Education Code.

11 (b) Except as otherwise provided in subdivision (c), gross  
12 income of a beneficiary or a participant does not include any of the  
13 following:

14 (1) Any distribution or earnings under a Scholarshare trust  
15 participation agreement, as provided in Article 19 (commencing  
16 with Section 69980) of Chapter 2 of Part 42 of the Education Code.

17 (2) Any contribution to the Scholarshare trust on behalf of a  
18 beneficiary shall not be includable as gross income of that  
19 beneficiary.

20 (c) (1) Any distribution under a Scholarshare trust  
21 participation agreement shall be includable in the gross income of  
22 the distributee in the manner as provided under Section 72 of the  
23 Internal Revenue Code, as modified by Section 17085, to the  
24 extent not excluded from gross income under this part. For  
25 purposes of applying Section 72 of the Internal Revenue Code, the  
26 following apply:

27 (A) All Scholarshare trust accounts of which an individual is a  
28 beneficiary shall be treated as one account, except as otherwise  
29 provided.

30 (B) All distributions during a taxable year shall be treated as  
31 one distribution.

32 (C) The value of the participation agreement, income on the  
33 participation agreement, and investment in the participation  
34 agreement shall be computed as of the close of the calendar year  
35 in which the taxable year begins.

36 (2) A contribution by a for-profit or nonprofit entity, or by a  
37 state or local government agency, for the benefit of an owner or  
38 employee of that entity or a beneficiary whom the owner or  
39 employee has the power to designate, including the owner or



1 employee's minor children, shall be included in the gross income  
2 of that owner or employee in the year the contribution is made.

3 (3) For purposes of this subdivision, "distribution" includes  
4 any benefit furnished to a beneficiary under a participation  
5 agreement, as provided in Article 19 (commencing with Section  
6 69980) of Chapter 2 of Part 42 of the Education Code.

7 (4) (A) Paragraph (1) shall not apply to that portion of any  
8 distribution that, within 60 days of distribution, is transferred to  
9 the credit of another beneficiary under the Scholarshare trust who  
10 is a "member of the family," as that term is used in Section  
11 529(e)(2) of the Internal Revenue Code, as amended by Section  
12 211 of the Taxpayer Relief Act of 1997 (Public Law 105-34), of  
13 the former beneficiary of that Scholarshare trust.

14 (B) Any change in the beneficiary of an interest in the  
15 Scholarshare trust shall not be treated as a distribution for purposes  
16 of paragraph (1) if the new beneficiary is a "member of the  
17 family," as that term is used in Section 529(e)(2) of the Internal  
18 Revenue Code, as amended by Section 211 of the Taxpayer Relief  
19 Act of 1997 (Public Law 105-34), of the former beneficiary of that  
20 Scholarshare trust.

21 (d) For taxable years beginning on or after January 1, 2002,  
22 Sections 529(c) and 529(e) of the Internal Revenue Code, as  
23 amended by Section 402 of the Economic Growth and Tax Relief  
24 Reconciliation Act of 2001 (Public Law 107-16), shall apply in  
25 lieu of subdivisions (b) and (c) of this section.

26 ~~SEC. 8.—~~

27 *SEC. 12.* Section 17140.3 of the Revenue and Taxation Code  
28 is amended to read:

29 17140.3. Section 529 of the Internal Revenue Code, as  
30 amended by Section 402 of the Economic Growth and Tax Relief  
31 Reconciliation Act of 2001 (Public Law 107-16), relating to  
32 qualified state tuition programs, shall apply, except as otherwise  
33 provided.

34 (a) Section 529 (a) of the Internal Revenue Code is modified as  
35 follows:

36 (1) By substituting the phrase "under this part and Part 11  
37 (commencing with Section 23001)" in lieu of the phrase "under  
38 this subtitle."

39 (2) By substituting "Article 2 (commencing with Section  
40 23731)" in lieu of "Section 511."



(b) A copy of the report required to be filed with the Secretary of the Treasury under Section 529(d) of the Internal Revenue Code shall be filed with the Franchise Tax Board at the same time and in the same manner as specified in that section.

~~SEC. 9. Section 17144 of the Revenue and Taxation Code is amended to read:~~

~~17144. (a) Section 108(b)(2)(B) of the Internal Revenue Code, relating to general business credit, is modified by substituting “this part” in lieu of “Section 38 (relating to general business credit).”~~

~~(b) Section 108(b)(2)(G) of the Internal Revenue Code, relating to foreign tax credit carryovers, shall not apply.~~

~~(c) Section 108(b)(3)(B) of the Internal Revenue Code, relating to credit carryover reduction, is modified by substituting “11.1 cents” in lieu of “33 $\frac{1}{3}$  cents” in each place in which it appears. In the case where more than one credit is allowable under this part, the credits shall be reduced on a pro rata basis.~~

~~(d) Section 108(g)(3)(B) of the Internal Revenue Code, relating to adjusted tax attributes, is modified by substituting “(\$9)” in lieu of “(\$3).”~~

~~(e) (1) If a taxpayer makes an election for federal income tax purposes under Section 108(e) of the Internal Revenue Code, relating to treatment of discharge of qualified real property business indebtedness, a separate election shall not be allowed and the federal election shall be binding for purposes of this part.~~

~~(2) If a taxpayer has not made an election for federal income tax purposes under Section 108(e) of the Internal Revenue Code, relating to treatment of discharge of qualified real property business indebtedness, then the taxpayer shall not be allowed to make that election for purposes of this part.~~

~~SEC. 10.—~~

~~SEC. 13. Section 17144.5 is added to the Revenue and Taxation Code, to read:~~

~~17144.5. Section 132 of the Internal Revenue Code, as amended by Title VI of the Economic Growth and Tax Relief Reconciliation Act of 2001 (Public Law 107-16), shall apply except as otherwise provided.~~

~~SEC. 11. Section 17152 of the Revenue and Taxation Code is amended to read:~~

1     ~~17152. — Section 121 of the Internal Revenue Code, relating to~~  
2     ~~exclusion of gain from sale of principal residence, is modified as~~  
3     ~~follows:~~

4     ~~(a) The two-year period in Section 121(a) of the Internal~~  
5     ~~Revenue Code shall be reduced by the period of the taxpayer's~~  
6     ~~service, not to exceed 18 months, in the Peace Corps during the~~  
7     ~~five-year period ending on the date of the sale or exchange.~~

8     ~~(b) If the taxpayer is prohibited from filing a joint return~~  
9     ~~pursuant to Section 18521, Section 121(b)(2)(A) of the Internal~~  
10    ~~Revenue Code shall nevertheless be treated as being satisfied if the~~  
11    ~~taxpayer files a joint return for federal income tax purposes for the~~  
12    ~~same taxable year. However, in no instance shall the total amount~~  
13    ~~excludable from gross income under Section 121(a) of the Internal~~  
14    ~~Revenue Code with respect to any sale or exchange exceed the~~  
15    ~~maximum amount allowed by Section 121(b) of the Internal~~  
16    ~~Revenue Code.~~

17    ~~(c) (1) If a taxpayer has, at any time, made an election for~~  
18    ~~federal income tax purposes under Section 121(f) of the Internal~~  
19    ~~Revenue Code not to have Section 121 of the Internal Revenue~~  
20    ~~Code apply to a sale or exchange, Section 121 of the Internal~~  
21    ~~Revenue Code shall not apply to that sale or exchange for state~~  
22    ~~purposes, a separate election for state purposes shall not be~~  
23    ~~allowed and the federal election shall be binding for purposes of~~  
24    ~~this part, and that election shall be treated as an election to include~~  
25    ~~in gross income for purposes of this part all the gain from the sale~~  
26    ~~or exchange of that property, including that amount which, but for~~  
27    ~~that election, would have been excluded from income under~~  
28    ~~Section 121(a) of the Internal Revenue Code for state purposes.~~

29    ~~(2) If a taxpayer fails to make an election for federal income tax~~  
30    ~~purposes under Section 121(f) of the Internal Revenue Code to not~~  
31    ~~have Section 121 of the Internal Revenue Code apply to a sale or~~  
32    ~~exchange, no election under Section 121(f) of the Internal~~  
33    ~~Revenue Code shall be allowed for state purposes, Section 121 of~~  
34    ~~the Internal Revenue Code shall apply to that sale or exchange for~~  
35    ~~state purposes, and a separate election for state purposes shall not~~  
36    ~~be allowed.~~

37    ~~(d) (1) If a taxpayer has, at any time, made an election for~~  
38    ~~federal income tax purposes under Section 312(d)(2) of the~~  
39    ~~Taxpayer Relief Act of 1997 (Public Law 105-34), relating to sales~~  
40    ~~before date of enactment, or Section 312(d)(4) of that act, relating~~

~~to binding contracts, to not have the amendments made by Section 312 of the Taxpayer Relief Act of 1997 (Public Law 105-34) apply to a sale or exchange, the amendments made by the act adding this subdivision shall not apply to that sale or exchange, Sections 1, 4, and 6 of Chapter 610 of the Statutes of 1997 shall not apply to that sale or exchange, a separate election for state purposes shall not be allowed and the federal election shall be binding for purposes of this part.~~

~~(2) If a taxpayer fails to make an election for federal income tax purposes under Section 312(d)(2) of the Taxpayer Relief Act of 1997 (Public Law 105-34), relating to sales before date of enactment, or Section 312(d)(4) of that act, relating to binding contracts, to not have the amendments made by Section 312 of the Taxpayer Relief Act of 1997 (Public Law 105-34) apply to a sale or exchange, an election under Section 312(d)(2) of the Taxpayer Relief Act of 1997 (Public Law 105-34), relating to sales before date of enactment, or Section 312(d)(4) of that act, relating to binding contracts, shall not be allowed for state purposes, the amendments made by the act adding this subdivision shall apply to that sale or exchange, Sections 1, 4, and 6 of Chapter 610 of the Statutes of 1997 shall apply to that sale or exchange, and a separate election for state purposes shall not be allowed.~~

~~SEC. 12.—~~

~~SEC. 14.~~ Section 17205 is added to the Revenue and Taxation Code, to read:

~~17205.~~ Section 219 of the Internal Revenue Code, as amended by Title VI of the Economic Growth and Tax Relief Reconciliation Act of 2001 (Public Law 107-16), relating to retirement savings, shall apply, except as otherwise provided.

~~SEC. 13.~~ ~~Section 17207.5 is added to the Revenue and Taxation Code, to read:~~

~~17207.5.~~ ~~Notwithstanding subdivision (e) of Section 17024.5, a taxpayer may make a separate state election, under Section 165(i)(1) of the Internal Revenue Code, to take a loss attributable to a disaster into account in the taxable year immediately preceding the taxable year in which the disaster occurred.~~

~~SEC. 14.~~ ~~Section 17279 of the Revenue and Taxation Code is amended to read:~~

1 17279. Section 197 of the Internal Revenue Code, relating to  
2 amortization of goodwill and certain other intangibles, is modified  
3 as follows:

4 (a) (1) Section 13261(g) of the Revenue Reconciliation Act of  
5 1993 (Public Law 103-66), relating to effective dates, shall apply,  
6 except as otherwise provided.

7 (2) (A) If a taxpayer has, at any time, made an election for  
8 federal income tax purposes under Section 13261(g)(2) of the  
9 Revenue Reconciliation Act of 1993 (Public Law 103-66),  
10 relating to election to have amendments apply to property acquired  
11 after July 25, 1991, or Section 13261(g)(3) of that act, relating to  
12 elective binding contract exception, a separate election for state  
13 purposes shall not be allowed and the federal election shall be  
14 binding for purposes of this part.

15 (B) If a taxpayer has not made an election for federal income  
16 tax purposes under Section 13261(g)(2) of the Revenue  
17 Reconciliation Act of 1993 (Public Law 103-66), relating to  
18 election to have amendments apply to property acquired after July  
19 25, 1991, or Section 13261(g)(3) of that act, relating to elective  
20 binding contract exception, with respect to property acquired  
21 before August 11, 1993, then the taxpayer shall not be allowed to  
22 make an election under Section 13261(g) of the Revenue  
23 Reconciliation Act of 1993 (Public Law 103-66), for purposes of  
24 this part, with respect to that property.

25 (b) Notwithstanding any other provision of this section, each of  
26 the following shall apply:

27 (1) No deduction shall be allowed under this section for any  
28 taxable year beginning prior to January 1, 1994.

29 (2) No inference is intended with respect to the allowance or  
30 denial of any deduction for amortization in any taxable year  
31 beginning before January 1, 1994.

32 (3) In the case of an intangible that was acquired in a taxable  
33 year beginning before January 1, 1994, the amount to be amortized  
34 shall not exceed the adjusted basis of that intangible as of the first  
35 day of the first taxable year beginning on or after January 1, 1994,  
36 and that amount shall be amortized ratably over the period  
37 beginning with the first month of the first taxable year beginning  
38 on or after January 1, 1994, and ending 15 years after the month  
39 in which the intangible was acquired.

~~SEC. 15.—Section 17279.4 of the Revenue and Taxation Code is amended to read:~~

~~17279.4.—Section 198 of the Internal Revenue Code, relating to expensing of environmental remediation costs, is modified as follows:~~

~~(a) (1) If a taxpayer has, at any time, made an election for federal income tax purposes under Section 198(a) of the Internal Revenue Code to have Section 198 of the Internal Revenue Code apply to a qualified environmental remediation expenditure, Section 198 of the Internal Revenue Code shall apply to that qualified environmental remediation expenditure for state purposes, a separate election for state purposes shall not be allowed and the federal election shall be binding for purposes of this part.~~

~~(2) If a taxpayer fails to make an election for federal income tax purposes under Section 198(a) of the Internal Revenue Code to have Section 198 of the Internal Revenue Code apply to a qualified environmental remediation expenditure, an election under Section 198(a) of the Internal Revenue Code shall not be allowed for state purposes, Section 198 of the Internal Revenue Code shall not apply to that qualified environmental remediation expenditure for state purposes, and a separate election for state purposes shall not be allowed.~~

~~(b) No inference as to the proper treatment for purposes of this part of qualified environmental remediation expenditures for periods before the enactment of this section shall be made.~~

~~SEC. 16.—~~

~~SEC. 15. Section 17271 of the Revenue and Taxation Code is repealed.~~

~~17271.—Section 274(a)(3) of the Internal Revenue Code, relating to denial of deduction for club dues, shall not apply.~~

~~SEC. 16. Section 17275.5 of the Revenue and Taxation Code is amended to read:~~

~~17275.5. (a) No deduction shall be denied under Section 170(f)(8) of the Internal Revenue Code, relating to substantiation requirement for certain contributions, upon a showing that the requirements in Section 170(f)(8) of the Internal Revenue Code have been met with respect to that contribution for federal purposes.~~

(b) Section 170(f)(9) of the Internal Revenue Code, relating to denial of deduction where contribution for lobbying activities, shall not apply.

*(c) Section 170(f)(10)(F) of the Internal Revenue Code, relating to excise tax on premiums paid, shall not apply.*

*SEC. 17. Section 17279.5 of the Revenue and Taxation Code is repealed.*

~~17279.5.—Section 264 of the Internal Revenue Code, relating to certain amounts paid in connection with insurance contracts, is modified to read as follows:~~

~~(a) No deduction shall be allowed for—~~

~~(1) Premiums on any life insurance policy, or endowment or annuity contract, if the taxpayer is directly or indirectly a beneficiary under the policy or contract.~~

~~(2) Any amount paid or accrued on indebtedness incurred to purchase or carry a single premium life insurance, endowment, or annuity contract. This paragraph shall apply with respect to annuity contracts only as to contracts purchased after December 31, 1954.~~

~~(3) Except as provided in subdivision (c), any amount paid or accrued on indebtedness incurred or continued to purchase or carry a life insurance, endowment, or annuity contract (other than a single premium contract or a contract treated as a single premium contract) pursuant to a plan of purchase which contemplates the systematic direct or indirect borrowing of part or all of the increases in the cash value of that contract (either from the insurer or otherwise). This paragraph shall apply only with respect to contracts purchased after August 6, 1963.~~

~~(4) Except as provided in subdivision (d), any interest paid or accrued on any indebtedness with respect to one or more insurance policies owned by the taxpayer covering the life of any individual, or any endowment or annuity contracts owned by the taxpayer covering the life of any individual, or any endowment or annuity contracts owned by the taxpayer covering any individual.~~

~~This paragraph shall apply with respect to contracts purchased after June 20, 1986.~~

~~(b) Paragraph (1) of subdivision (a) shall not apply to either of the following:~~

~~(1) Any annuity contract described in Section 72(s)(5) of the Internal Revenue Code.~~



1 ~~(2) Any annuity contract to which Section 72(u) of the Internal~~  
2 ~~Revenue Code applies.~~

3 ~~(e) For purposes of paragraph (2) of subdivision (a), a contract~~  
4 ~~shall be treated as a single premium contract if either of the~~  
5 ~~following conditions exist:~~

6 ~~(1) Substantially all the premiums on the contract are paid~~  
7 ~~within a period of four years from the date on which the contract~~  
8 ~~is purchased.~~

9 ~~(2) An amount is deposited after December 31, 1954, with the~~  
10 ~~insurer for payment of a substantial number of future premiums on~~  
11 ~~the contract.~~

12 ~~(d) Paragraph (3) of subdivision (a) shall not apply to any~~  
13 ~~amount paid or accrued by a person during a taxable year on~~  
14 ~~indebtedness incurred or continued as part of a plan referred to in~~  
15 ~~paragraph (3) of subdivision (a) if any of the following are~~  
16 ~~applicable:~~

17 ~~(1) No part of four of the annual premiums due during the~~  
18 ~~seven-year period (beginning with the date the first premium on~~  
19 ~~the contract to which that plan relates was paid) is paid under that~~  
20 ~~plan by means of indebtedness.~~

21 ~~(2) The total of the amounts paid or accrued by the person~~  
22 ~~during that taxable year for which (without regard to this~~  
23 ~~paragraph) no deduction would be allowable by reason of~~  
24 ~~paragraph (3) of subdivision (a) does not exceed one hundred~~  
25 ~~dollars (\$100).~~

26 ~~(3) That amount was paid or accrued on indebtedness incurred~~  
27 ~~because of an unforeseen substantial loss of income or unforeseen~~  
28 ~~substantial increase in its financial obligations.~~

29 ~~(4) That indebtedness was incurred in connection with its trade~~  
30 ~~or business.~~

31 ~~For purposes of applying paragraph (1), if there is a substantial~~  
32 ~~increase in the premiums on a contract, a new seven-year period~~  
33 ~~described in that paragraph with respect to that contract shall~~  
34 ~~commence on the date the first that increased premium is paid.~~

35 ~~(e) (1) Paragraph (4) of subdivision (a) shall not apply to any~~  
36 ~~interest paid or accrued on any indebtedness with respect to~~  
37 ~~policies or contracts covering an individual who is a key person to~~  
38 ~~the extent that the aggregate amount of that indebtedness with~~  
39 ~~respect to policies and contracts covering that individual does not~~  
40 ~~exceed fifty thousand dollars (\$50,000).~~

~~(2) (A) No deduction shall be allowed by reason of paragraph (1) or the last sentence of subdivision (a) with respect to interest paid or accrued for any month beginning after December 31, 1995, to the extent the amount of that interest exceeds the amount which would have been determined if the applicable rate of interest were used for that month.~~

~~(B) For purposes of subparagraph (A):~~

~~(i) The applicable rate of interest for any month is the rate of interest described as Moody's Corporate Bond Yield Average Monthly Average Corporates, as published by Moody's Investors Service, Inc., or any successor thereto, for that month.~~

~~(ii) In the case of indebtedness on a contract purchased on or before June 20, 1986, all of the following shall apply:~~

~~(I) If the contract provides a fixed rate of interest, the applicable rate of interest for any month shall be the Moody's rate described in clause (i) for the month in which the contract was purchased.~~

~~(II) If the contract provides a variable rate of interest, the applicable rate of interest for any month in an applicable period shall be the Moody's rate described in clause (i) for the third month preceding the first month in that period.~~

~~(III) For purposes of subclause (II), the term "applicable period" means the 12-month period beginning on the date the policy is issued (and each successive 12-month period thereafter) unless the taxpayer elects a number of months (not greater than 12) other than that 12-month period to be its applicable period. That election shall be made not later than the 90th day after the date of the enactment of the act adding this sentence and, if made, shall apply to the taxpayer's first taxable year ending on or after December 31, 1995, and all subsequent taxable years unless revoked with the consent of the Franchise Tax Board.~~

~~(3) For purposes of paragraph (1), "key person" means an officer or 20-percent owner, except that the number of individuals who may be treated as key persons with respect to any taxpayer shall not exceed the greater of:~~

~~(A) Five individuals.~~

~~(B) The lesser of 5 percent of the total officers and employees of the taxpayer or 20 individuals.~~

~~(4) For purposes of this subdivision, "20-percent owner" means both of the following:~~

1 ~~(A) If the taxpayer is a corporation, any person who owns~~  
2 ~~directly 20 percent or more of the outstanding stock of the~~  
3 ~~corporation or stock possessing 20 percent or more of the total~~  
4 ~~combined voting power of all stock of the corporation.~~

5 ~~(B) If the taxpayer is not a corporation, any person who owns~~  
6 ~~20 percent or more of the capital or profits interest in the taxpayer.~~

7 ~~(5) (A) For purposes of subparagraph (A) of paragraph (4) and~~  
8 ~~for purposes of applying the fifty thousand dollar (\$50,000)~~  
9 ~~limitation in paragraph (1) both of the following shall apply:~~

10 ~~(i) All members of a controlled group shall be treated as one~~  
11 ~~taxpayer.~~

12 ~~(ii) The limitation shall be allocated among the members of the~~  
13 ~~controlled group in the manner the Franchise Tax Board may~~  
14 ~~prescribe.~~

15 ~~(B) For purposes of this paragraph, all persons treated as a~~  
16 ~~single employer under Section 52(a) or 52(b) of the Internal~~  
17 ~~Revenue Code, relating to special rules, or Section 414(m) or~~  
18 ~~414(o) of the Internal Revenue Code, relating to definitions and~~  
19 ~~special rules, shall be treated as members of a controlled group.~~

20 ~~(f) (1) No deduction shall be allowed for that portion of the~~  
21 ~~taxpayer's interest expense which is allocable to unborrowed~~  
22 ~~policy cash values.~~

23 ~~(2) For purposes of paragraph (1), the portion of the taxpayer's~~  
24 ~~interest expense which is allocable to unborrowed policy cash~~  
25 ~~values is an amount which bears the same ratio to the interest~~  
26 ~~expense as:~~

27 ~~(A) The taxpayer's average unborrowed policy cash values of~~  
28 ~~life insurance policies, and annuity and endowment contracts,~~  
29 ~~issued after June 8, 1997, bears to~~

30 ~~(B) The sum of:~~

31 ~~(i) In the case of assets of the taxpayer which are life insurance~~  
32 ~~policies or annuity or endowment contracts, the average~~  
33 ~~unborrowed policy cash values of those policies and contracts, and~~

34 ~~(ii) In the case of assets of the taxpayer not described in clause~~  
35 ~~(i), the average adjusted bases (within the meaning of Section 1016~~  
36 ~~of the Internal Revenue Code) of those assets.~~

37 ~~(3) For purposes of this subdivision, the term "unborrowed~~  
38 ~~policy cash value" means, with respect to any life insurance policy~~  
39 ~~or annuity or endowment contract, the excess of:~~

~~(A) The cash surrender value of the policy or contract determined without regard to any surrender charge, over~~

~~(B) The amount of any loan with respect to that policy or contract.~~

~~(4) (A) Paragraph (1) shall not apply to any policy or contract owned by an entity engaged in a trade or business if the policy or contract covers only one individual and if that individual is (at the time first covered by the policy or contract):~~

~~(i) A 20-percent owner of the entity, or~~

~~(ii) An individual (not described in clause (i)) who is an officer, director, or employee of that trade or business.~~

~~A policy or contract covering a 20-percent owner of the entity shall not be treated as failing to meet the requirements of the preceding sentence by reason of covering the joint lives of the owner and the owner's spouse.~~

~~(B) Paragraph (1) shall not apply to any annuity contract to which Section 72(u) of the Internal Revenue Code applies.~~

~~(C) Any policy or contract to which paragraph (1) does not apply by reason of this paragraph shall not be taken into account under paragraph (2).~~

~~(D) For purposes of subparagraph (A), the term "20-percent owner" has the meaning given that term by paragraph (4) of subdivision (e).~~

~~(5) (A) (i) This subdivision shall not apply to any policy or contract held by a natural person.~~

~~(ii) If a trade or business is directly or indirectly the beneficiary under any policy or contract, the policy or contract shall be treated as held by that trade or business and not by a natural person.~~

~~(iii) (I) Clause (ii) shall not apply to any trade or business carried on as a sole proprietorship and to any trade or business performing services as an employee.~~

~~(H) The amount of the unborrowed cash value of any policy or contract which is taken into account by reason of clause (ii) shall not exceed the benefit to which the trade or business is directly or indirectly entitled under the policy or contract.~~

~~(iv) A copy of the report required for federal purposes under Section 264(f) of the Internal Revenue Code shall be filed with the Franchise Tax Board at the time and in the manner specified for federal purposes and shall be treated as a statement referred to in Section 6724(d)(1) of the Internal Revenue Code.~~

1 ~~(B) In the case of a partnership or S corporation, this~~  
2 ~~subdivision shall be applied at the partnership and corporate~~  
3 ~~levels.~~

4 ~~(6) (A) If interest on any indebtedness is disallowed under~~  
5 ~~subdivision (a) or Section 17280, both of the following shall apply:~~

6 ~~(i) The disallowed interest shall not be taken into account for~~  
7 ~~purposes of applying this subdivision.~~

8 ~~(ii) The amount otherwise taken into account under~~  
9 ~~subparagraph (B) of paragraph (2) shall be reduced (but not below~~  
10 ~~zero) by the amount of the indebtedness.~~

11 ~~(B) This subdivision shall be applied before the application of~~  
12 ~~Section 263A of the Internal Revenue Code, relating to~~  
13 ~~capitalization of certain expenses where taxpayer produces~~  
14 ~~property.~~

15 ~~(7) The term “interest expense” means the aggregate amount~~  
16 ~~allowable to the taxpayer as a deduction for interest (within the~~  
17 ~~meaning of Section 265(b)(4) of the Internal Revenue Code) for~~  
18 ~~the taxable year (determined without regard to this subdivision,~~  
19 ~~Section 265(b) of the Internal Revenue Code, and Section 291 of~~  
20 ~~the Internal Revenue Code).~~

21 ~~(8) All members of a controlled group (within the meaning of~~  
22 ~~subparagraph (B) of paragraph (5) of subdivision (c)) shall be~~  
23 ~~treated as one taxpayer for purposes of this subdivision.~~

24 ~~(g) (1) The amendments made to this section by the act adding~~  
25 ~~this subdivision shall apply to interest paid or accrued after~~  
26 ~~December 31, 1995.~~

27 ~~(2) (A) The amendments made to this section by the act adding~~  
28 ~~this subdivision shall not apply to qualified interest paid or accrued~~  
29 ~~on that indebtedness after December 31, 1995, and before January~~  
30 ~~1, 1999, in the case of either of the following:~~

31 ~~(i) Indebtedness incurred before January 1, 1996.~~

32 ~~(ii) Indebtedness incurred before January 1, 1997, with respect~~  
33 ~~to any contract or policy entered into in 1994 or 1995.~~

34 ~~(B) For purposes of subparagraph (A), the qualified interest~~  
35 ~~with respect to any indebtedness for any month is the amount of~~  
36 ~~interest (otherwise deductible) which would be paid or accrued for~~  
37 ~~that month on that indebtedness if—~~

38 ~~(i) In the case of any interest paid or accrued after December~~  
39 ~~31, 1995, indebtedness with respect to no more than 20,000~~  
40 ~~insured individuals were taken into account, and~~

~~(ii) The lesser of the following rates of interest were used for that month:~~

~~(I) The rate of interest specified under the terms of the indebtedness as in effect on December 31, 1995 (and without regard to modification of the terms after that date).~~

~~(II) The applicable percentage of the rate of interest described as Moody's Corporate Bond Yield Average Monthly Average Corporates, as published by Moody's Investors Service, Inc., or any successor thereto, for that month. For purposes of clause (i), all persons treated as a single employer under Section 52(a) or 52(b) of the Internal Revenue Code, relating to special rules, or Section 414(m) or 414(o) of the Internal Revenue Code, relating to definitions and special rules, shall be treated as one person. Subclause (II) of clause (ii) shall not apply to any month before January 1, 1996.~~

~~(C) For purposes of subparagraph (B), the applicable percentage is as follows:~~

<del>For calendar year:</del>	<del>The percentage is:</del>
<del>1996 .....</del>	<del>100 percent</del>
<del>1997 .....</del>	<del>90 percent</del>
<del>1998 .....</del>	<del>80 percent</del>

~~(3) This subdivision shall not apply to any contract purchased on or before June 20, 1986, except that paragraph (2) of subdivision (d) shall apply to interest paid or accrued after December 31, 1995.~~

~~(h) (1) Any amount received under any life insurance policy or endowment or annuity contract described in paragraph (4) of subdivision (a) shall be includable in gross income (in lieu of any other inclusion in gross income) ratably over the four taxable year period beginning with the taxable year that amount would (but for this paragraph) be includable, upon the occurrence of either of the following:~~

~~(A) The complete surrender, redemption, or maturity of that policy or contract during the calendar year 1996, 1997, or 1998.~~

~~(B) The full discharge during calendar year 1996, 1997, or 1998, of the obligation under the policy or contract which is in the nature of a refund of the consideration paid for the policy or contract.~~

~~(2) Paragraph (1) shall only apply to the extent the amount is includable in gross income for the taxable year in which the event described in subparagraph (A) or (B) of paragraph (1) occurs.~~

~~(3) Solely by reason of an occurrence described in subparagraph (A) or (B) of paragraph (1) or solely by reason of no additional premiums being received under the contract by reason of a lapse occurring after December 31, 1995, a contract shall not be treated as either of the following:~~

~~(A) Failing to meet the requirement of paragraph (1) of subdivision (c).~~

~~(B) A single premium contract under paragraph (1) of subdivision (b).~~

~~(i) The amendments made by the act adding this subdivision shall apply to contracts issued after June 8, 1997, in taxable years beginning on or after January 1, 1998. For purposes of the preceding sentence, any material increase in the death benefit or other material change in the contract shall be treated as a new contract, except that the addition of covered lives shall be treated as a new contract only with respect to those additional covered lives. For purposes of this subdivision, an increase in the death benefit under a policy or contract issued in connection with a lapse described in Section 501(d)(2) of the Health Insurance Portability and Accountability Act of 1996 shall not be treated as a new contract.~~

*SEC. 18.* Section 17501 of the Revenue and Taxation Code is amended to read:

17501. (a) Subchapter D of Chapter 1 of Subtitle A of the Internal Revenue Code, relating to deferred compensation, shall apply, except as otherwise provided.

(b) Notwithstanding Section 17024.5, Part I of Subchapter D of Chapter 1 of Subtitle A of the Internal Revenue Code, relating to pension, profit sharing, stock bonus plans, etc., shall apply, except as otherwise provided, without regard to taxable year to the same extent as applicable for federal purposes.

(c) The maximum amount of elective deferrals (as defined in Section 402(g)(3)) for the taxable year that may be excluded from gross income under Section 403(g) of the Internal Revenue Code, as applicable for state purposes, shall not exceed the amount of elective deferrals that may be excluded from gross income under Section 402(g) of the Internal Revenue Code, as amended by Title



1 VI of the Economic Growth and Tax Relief Reconciliation Act of  
2 2001 (Public Law 107-16), including additional elective deferrals  
3 under Section 414(v) of the Internal Revenue Code, as added by  
4 Title VI of the Economic Growth and Tax Relief Reconciliation  
5 Act of 2001 (Public Law 107-16).

6 (d) (1) For taxable years beginning on or after January 1, 2002,  
7 the basis of any person in the plan, account, or annuity shall be  
8 increased by the amount of elective deferrals not excluded as a  
9 result of the application of subdivision (c).

10 (2) Any basis described in paragraph (1) shall be recovered in  
11 the manner specified in Section 17085.

12 (e) Notwithstanding the limitations provided in subdivision  
13 (c), any income attributable to elective deferrals in taxable years  
14 beginning on or after January 1, 2002, in conformance with Part  
15 I of Subchapter D of Chapter 1 of Subtitle A of the Internal  
16 Revenue Code, as applicable for federal and state purposes, shall  
17 not be includable in the gross income of the individual for whose  
18 benefit the plan or account was established until distributed  
19 pursuant to the provisions of the plan or by operation of law.

20 ~~SEC. 17.—~~

21 *SEC. 19.* Section 17551 of the Revenue and Taxation Code is  
22 amended to read:

23 17551. (a) Subchapter E of Chapter 1 of Subtitle A of the  
24 Internal Revenue Code, relating to accounting periods and  
25 methods of accounting, shall apply, except as otherwise provided.

26 (b) Section 444(c)(1) of the Internal Revenue Code, relating to  
27 effect of election, shall not apply.

28 (c) (1) Notwithstanding Section 17024.5, Section 457 of the  
29 Internal Revenue Code, relating to deferred compensation plans of  
30 state and local governments and tax-exempt organizations, shall  
31 apply, except as otherwise provided, without regard to taxable year  
32 to the same extent as applicable for federal purposes.

33 (2) The maximum deferred compensation for the taxable year  
34 that may be excluded from gross income under Section 457 of the  
35 Internal Revenue Code shall not exceed the amount of deferred  
36 compensation that may be excluded from gross income under  
37 Section 457 of the Internal Revenue Code, as amended by Title VI  
38 of the Economic Growth and Tax Relief Reconciliation Act of  
39 2001 (Public Law 107-16), including additional elective deferrals  
40 under Section 414(v) of the Internal Revenue Code, as added by

1 Title VI of the Economic Growth and Tax Relief Reconciliation  
2 Act of 2001 (Public Law 107-16).

3 (d) (1) For taxable years beginning on or after January 1, 2002,  
4 the basis of any person in the plan shall be increased by the amount  
5 of compensation not allowed to be excluded under subdivision (a).

6 (2) Any basis described in paragraph (1) shall be recovered in  
7 the manner specified in Section 17085.

8 (e) Notwithstanding the limitations provided in subdivision  
9 (a), any income attributable to compensation deferred in a plan in  
10 taxable years beginning on or after January 1, 2002, in  
11 conformance with Section 457 of the Internal Revenue Code, as  
12 applicable for federal and state purposes, shall not be includable  
13 in the gross income of the individual for whose benefit the plan was  
14 established until distributed pursuant to the provisions of the plan  
15 or by operation of law.

16 ~~SEC. 18. Section 17570 of the Revenue and Taxation Code is~~  
17 ~~amended to read:~~

18 ~~17570. (a) For each taxable year beginning on or after~~  
19 ~~January 1, 1997, Section 475 of the Internal Revenue Code,~~  
20 ~~relating to mark to market accounting method for securities~~  
21 ~~dealers, shall apply, except as otherwise provided.~~

22 ~~(b) Section 13233(c)(2)(C) of the Revenue Reconciliation Act~~  
23 ~~of 1993 (Public Law 103-66), relating to the effective date for~~  
24 ~~changes in the mark to market accounting method for securities~~  
25 ~~dealers, is modified to provide that the amount taken into account~~  
26 ~~under Section 481 of the Internal Revenue Code of 1986 shall be~~  
27 ~~taken into account ratably over the five-taxable-year period~~  
28 ~~beginning with the first taxable year beginning on or after January~~  
29 ~~1, 1997.~~

30 ~~(c) (1) If a taxpayer has, at any time, made an election for~~  
31 ~~federal income tax purposes under Section 475(e) of the Internal~~  
32 ~~Revenue Code, relating to election of mark to market for dealers~~  
33 ~~in commodities, to have Section 475 of the Internal Revenue Code~~  
34 ~~apply, Section 475 of the Internal Revenue Code shall apply to that~~  
35 ~~dealer in commodities for state purposes, a separate election for~~  
36 ~~state purposes shall not be allowed and the federal election shall~~  
37 ~~be binding for purposes of this part.~~

38 ~~(2) If a taxpayer fails to make, or has not previously made, an~~  
39 ~~election for federal income tax purposes under Section 475(e) of~~  
40 ~~the Internal Revenue Code, relating to election of mark to market~~

1 ~~for dealers in commodities, to have Section 475 of the Internal~~  
2 ~~Revenue Code apply, an election under Section 475(e) of the~~  
3 ~~Internal Revenue Code shall not be allowed for state purposes,~~  
4 ~~Section 475 of the Internal Revenue Code shall not apply to that~~  
5 ~~dealer in commodities for state purposes, and a separate election~~  
6 ~~for state purposes shall not be allowed.~~

7 ~~(d) (1) If a taxpayer has, at any time, made an election for~~  
8 ~~federal income tax purposes under Section 475(f)(1) of the~~  
9 ~~Internal Revenue Code, relating to election of mark to market for~~  
10 ~~traders in securities, to have Section 475 of the Internal Revenue~~  
11 ~~Code apply to a trade or business, Section 475 of the Internal~~  
12 ~~Revenue Code shall apply to that trader in securities for state~~  
13 ~~purposes with respect to that trade or business, a separate election~~  
14 ~~for state purposes with respect to that trade or business shall not be~~  
15 ~~allowed and the federal election shall be binding for purposes of~~  
16 ~~this part.~~

17 ~~(2) If a taxpayer fails to make, or has not previously made, an~~  
18 ~~election for federal income tax purposes under Section 475(f)(1)~~  
19 ~~of the Internal Revenue Code, relating to election of mark to~~  
20 ~~market for traders in securities, to have Section 475 of the Internal~~  
21 ~~Revenue Code apply to a trade or business, an election under~~  
22 ~~Section 475(f)(1) of the Internal Revenue Code shall not be~~  
23 ~~allowed for state purposes with respect to that trade or business,~~  
24 ~~Section 475 of the Internal Revenue Code shall not apply to that~~  
25 ~~trader in securities for state purposes with respect to that trade or~~  
26 ~~business, and a separate election for state purposes shall not be~~  
27 ~~allowed.~~

28 ~~(e) (1) If a taxpayer has, at any time, made an election for~~  
29 ~~federal income tax purposes under Section 475(f)(2) of the~~  
30 ~~Internal Revenue Code, relating to election of mark to market for~~  
31 ~~traders in commodities, to have Section 475 of the Internal~~  
32 ~~Revenue Code apply to a trade or business, Section 475 of the~~  
33 ~~Internal Revenue Code shall apply to that trader in commodities~~  
34 ~~for state purposes with respect to that trade or business, a separate~~  
35 ~~election for state purposes with respect to that trade or business~~  
36 ~~shall not be allowed and the federal election with respect to that~~  
37 ~~trade or business shall be binding for purposes of this part.~~

38 ~~(2) If a taxpayer fails to make, or has not previously made, an~~  
39 ~~election for federal income tax purposes under Section 475(f)(2)~~  
40 ~~of the Internal Revenue Code, relating to election of mark to~~

~~market for traders in commodities, to have Section 475 of the Internal Revenue Code apply to a trade or business, an election under Section 475(f)(2) of the Internal Revenue Code shall not be allowed for state purposes with respect to that trade or business, Section 475 of the Internal Revenue Code shall not apply to that trader in commodities for state purposes with respect to that trade or business, and a separate election for state purposes with respect to that trade or business shall not be allowed.~~

~~(f) (1) An election under Section 475(e) or (f) of the Internal Revenue Code made for federal income tax purposes with respect to a taxable year beginning before January 1, 1998, shall be treated as having been made for state purposes with respect to the first taxable year beginning on or after January 1, 1998.~~

~~(2) Section 1001(d)(4)(B) of the Taxpayer Relief Act of 1997 (Public Law 105-34), relating to the effective date for election of mark to market by securities traders and traders and dealers in commodities, is modified to provide that the requirement for timely identification shall be treated as timely made for state purposes if that identification is treated as timely made for federal income tax purposes, and the amount taken into account under Section 481 of the Internal Revenue Code of 1986 shall be taken into account ratably over the four-taxable-year period beginning with the first taxable year beginning on or after January 1, 1998.~~

~~SEC. 19. Section 17751 of the Revenue and Taxation Code is amended to read:~~

~~17751. Section 646 of the Internal Revenue Code, relating to certain revocable trusts treated as part of estate, is modified as follows:~~

~~(a) An election under Section 646(a) of the Internal Revenue Code for federal income tax purposes shall be treated for purposes of this part as an election made by the executor, if any, of the estate and the trustee of the qualified revocable trust under Section 646(a) of the Internal Revenue Code for state purposes and a separate election shall not be allowed.~~

~~(b) If the executor, if any, of the estate and the trustee of a qualified revocable trust fail to make an election under Section 646(a) of the Internal Revenue Code for federal income tax purposes with respect to that qualified revocable trust, that trust shall be treated and taxed for purposes of this part as a separate trust, an election under Section 646(a) of the Internal Revenue~~

~~Code for state purposes with respect to that trust shall not be allowed, and a separate election shall not be allowed with respect to that trust.~~

~~SEC. 20. Section 17752 of the Revenue and Taxation Code is amended to read:~~

~~17752. Section 663 of the Internal Revenue Code, relating to special rules applicable to Sections 661 and 662, is modified as follows:~~

~~(a) Section 663(b) of the Internal Revenue Code, relating to distributions in the first 65 days of the taxable year, is modified as follows:~~

~~(1) An election under Section 663(b) of the Internal Revenue Code for federal income tax purposes shall be treated for purposes of this part as an election made by the executor of the estate or the fiduciary of the trust, as the case may be, under Section 663(b) of the Internal Revenue Code for state purposes and a separate election shall not be allowed.~~

~~(2) If the executor of the estate or the fiduciary of the trust, as the case may be, fails to make an election under Section 663(b) of the Internal Revenue Code for federal income tax purposes with respect to an amount properly paid or credited within 65 days of the taxable year, that amount shall not be considered for purposes of this part as having been paid or credited on the last day of the preceding taxable year, an election under Section 663(b) of the Internal Revenue Code for state purposes with respect to that amount shall not be allowed, and a separate election shall not be allowed with respect to that amount.~~

~~(b) Section 663(c) of the Internal Revenue Code, relating to separate shares treated as separate estates or trusts, is modified as follows:~~

~~(1) An election under Section 663(c) of the Internal Revenue Code for federal income tax purposes shall be treated for purposes of this part as an election made by the executor of the estate or the fiduciary of the trust, as the case may be, under Section 663(c) of the Internal Revenue Code for state purposes and a separate election shall not be allowed.~~

~~(2) If the executor of the estate or the fiduciary of the trust, as the case may be, fails to make an election under Section 663(c) of the Internal Revenue Code for federal income tax purposes with respect to separate shares treated as separate estates or trusts, an~~

~~election under Section 663(c) of the Internal Revenue Code for state purposes shall not be allowed, and a separate election shall not be allowed.~~

~~SEC. 21.— Section 17760.5 of the Revenue and Taxation Code is amended to read:~~

~~17760.5.— Section 685 of the Internal Revenue Code, relating to treatment of funeral trusts, is modified as follows:~~

~~(a) Section 685(a) of the Internal Revenue Code is modified to read: In the case of a qualified funeral trust—~~

~~(1) Subparts B, C, D, and E of Subchapter J of Chapter 1 of Subtitle A of the Internal Revenue Code shall not apply.~~

~~(2) No credit for personal exemption shall be allowed under Section 17054 or Section 17733.~~

~~(b) Section 685(b) of the Internal Revenue Code is modified as follows:~~

~~(1) An election under Section 685(b)(5) of the Internal Revenue Code for federal income tax purposes shall be treated for purposes of this part as an election made by the trustee of the qualified funeral trust under Section 685(b)(5) of the Internal Revenue Code for state purposes and a separate election shall not be allowed.~~

~~(2) If the trustee of a qualified funeral trust fails to make an election under Section 685(b)(5) of the Internal Revenue Code for federal income tax purposes with respect to a qualified funeral trust, that trust shall be treated for purposes of this part as owned under Subpart E of the Internal Revenue Code by the purchasers of the contracts described in Section 685(b)(1) of the Internal Revenue Code, an election under Section 685(b)(5) of the Internal Revenue Code for state purposes with respect to that trust shall not be allowed, and a separate election shall not be allowed with respect to that trust.~~

~~(c) Section 685(d) of the Internal Revenue Code is modified to read: Subdivision (c) of Section 17041 shall be applied to each qualified funeral trust by treating each beneficiary's interest in each qualified funeral trust as a separate trust.~~

~~(d) The Franchise Tax Board may, by forms and instructions, provide rules for simplified reporting of all trusts having a single trustee consistent with the rules prescribed by the Secretary of the Treasury under Section 685 of the Internal Revenue Code.~~

~~(e) This section shall apply to taxable years ending after August 5, 1997.~~

~~(f) The amendments made to this section by the act adding this subdivision shall apply to taxable years beginning on or after January 1, 1998.~~

~~SEC. 21.2.—Section 18037 of the Revenue and Taxation Code is repealed.~~

~~SEC. 21.4.—Section 18521 of the Revenue and Taxation Code is amended to read:~~

~~18521.—(a) (1) Except as otherwise provided in this section, an individual shall use the same filing status that he or she used on his or her federal income tax return filed for the same taxable year.~~

~~(2) If the Franchise Tax Board determines that the filing status used on the taxpayer's federal income tax return was incorrect, the Franchise Tax Board may, under Section 19033 (relating to deficiency assessments), revise the return to reflect a correct filing status.~~

~~(3) If either spouse was a nonresident for any portion of the taxable year, a husband and wife who file a joint federal income tax return shall be required to file a joint nonresident return.~~

~~(b) In the case of an individual who is not required to file a federal income tax return for the taxable year, that individual may use any filing status on the return required under this part that he or she would be eligible to use on a federal income tax return for the same taxable year if a federal income tax return was required.~~

~~(c) Notwithstanding subdivision (a), a husband and wife may file separate returns under this part if either spouse was either of the following during the taxable year:~~

~~(1) An active member of the armed forces or any auxiliary branch thereof.~~

~~(2) A nonresident for the entire taxable year who had no income from a California source.~~

~~(d) Except for taxpayers described in subdivision (c), for any taxable year with respect to which a joint return has been filed, a separate return shall not be made by either spouse after the period for either to file a separate return has expired.~~

~~(e) No joint return shall be made if the husband and wife have different taxable years; except that if their taxable years begin on the same day and end on different days because of the death of either or both, then a joint return may be made with respect to the~~



1 taxable year of each. The above exception shall not apply if the  
2 surviving spouse remarries before the close of his or her taxable  
3 year, or if the taxable year of either spouse is a fractional part of  
4 a year under Section 443(a) of the Internal Revenue Code.

5 (f) ~~In the case of the death of one spouse or both spouses the~~  
6 ~~joint return with respect to the decedent may be made only by the~~  
7 ~~decedent's executor or administrator; except that, in the case of the~~  
8 ~~death of one spouse, the joint return may be made by the surviving~~  
9 ~~spouse with respect to both that spouse and the decedent if no~~  
10 ~~return for the taxable year has been made by the decedent, no~~  
11 ~~executor or administrator has been appointed, and no executor or~~  
12 ~~administrator is appointed before the last day prescribed by law for~~  
13 ~~filing the return of the surviving spouse. If an executor or~~  
14 ~~administrator of the decedent is appointed after the making of the~~  
15 ~~joint return by the surviving spouse and the executor disaffirms the~~  
16 ~~joint return made for federal income tax purposes pursuant to~~  
17 ~~Section 6013(a)(3) of the Internal Revenue Code, the executor or~~  
18 ~~administrator shall be deemed to have disaffirmed the joint return~~  
19 ~~made by the surviving spouse for purposes of Part 10~~  
20 ~~(commencing with Section 17001) and this part and shall make,~~  
21 ~~within one year after the last day prescribed by law for filing the~~  
22 ~~return of the surviving spouse, a separate return for the taxable~~  
23 ~~year of the decedent with respect to which the joint return was~~  
24 ~~made, in which case the return made by the survivor shall~~  
25 ~~constitute his or her separate return. If an executor or administrator~~  
26 ~~of the decedent is appointed after the making of the joint return by~~  
27 ~~the surviving spouse and the executor does not disaffirm the joint~~  
28 ~~return made for federal income tax purposes pursuant to Section~~  
29 ~~6013(a)(3) of the Internal Revenue Code, the executor or~~  
30 ~~administrator shall not be allowed to disaffirm the joint return~~  
31 ~~made by the surviving spouse for purposes of Part 10~~  
32 ~~(commencing with Section 17001) and this part.~~

33 ~~SEC. 22.—~~

34 *SEC. 20. Section 17552.3 is added to the Revenue and*  
35 *Taxation Code, to read:*

36 *17552.3. (a) (1) The options under Sections 112(d)(2) and*  
37 *112(d)(3) of the Federal Agriculture Improvement and Reform Act*  
38 *of 1996 (7 U.S.C. Sec. 7212(d)(2) and (3)), as in effect on October*  
39 *21, 1998, shall be disregarded in determining the taxable year for*  
40 *which any payment under a production flexibility contract under*

1 *Subtitle B of Title I of that act (as so in effect) is properly includable*  
2 *in gross income for purposes of this part, Part 10.2 (commencing*  
3 *with Section 18401) and Part 11 (commencing with Section*  
4 *23001).*

5 *(2) In order to provide farmers with the same tax treatment for*  
6 *all payments in years beginning before January 1, 2002, with*  
7 *respect to production flexibility contract payments as under*  
8 *federal law, as modified by Public Law 105-277, this subdivision*  
9 *shall apply to taxable years ending after December 31, 1995.*

10 *(b) Any option to accelerate the receipt of any payment under*  
11 *a production flexibility contract entered into on or after January*  
12 *1, 2002, which is payable under the Federal Agriculture*  
13 *Improvement and Reform Act of 1996 (7 U.S.C. Sec. 7200 et seq.),*  
14 *as in effect on December 17, 1999, shall be disregarded in*  
15 *determining the taxable year for which that payment is properly*  
16 *includable in gross income for purposes of this part, Part 10.2*  
17 *(commencing with Section 18401), and Part 11 (commencing with*  
18 *Section 23001).*

19 *SEC. 21. Section 17560 of the Revenue and Taxation Code is*  
20 *amended to read:*

21 *17560. (a) The provisions of Sections ~~811(e)(2)~~, 811(c)(4),*  
22 *811(c)(6), and 811(c)(7) of Public Law 99-514, as modified by*  
23 *Section 1008(f) of Public Law 100-647, shall apply.*

24 *(b) The provisions of Section 812 of Public Law 99-514,*  
25 *relating to the disallowance of use of installment method for*  
26 *certain obligations as modified by Section 1008(g) of Public Law*  
27 *100-647, shall apply to taxable years beginning on or after January*  
28 *1, 1987.*

29 *(c) The repeal of Section 453C of the Internal Revenue Code*  
30 *by Section 10202(a) of Public Law 100-203, relating to repeal of*  
31 *the proportionate disallowance of the installment method, shall*  
32 *apply to dispositions in taxable years beginning on or after January*  
33 *1, 1990.*

34 *(d) (1) In the case of any installment obligation to which*  
35 *Section 453(l)(2)(B) of the Internal Revenue Code applies, in lieu*  
36 *of the provisions of Section 453(l)(3)(A) of the Internal Revenue*  
37 *Code, the tax imposed under Section 17041 or 17048 for any*  
38 *taxable year for which payment is received on that obligation shall*  
39 *be increased by the amount of interest determined in the manner*

1 provided under Section 453(l)(3)(B) of the Internal Revenue  
2 Code.

3 (2) The provisions of Sections 10202 and 10204 of Public Law  
4 100-203 are modified to provide for each of the following:

5 (A) The provisions of Section 10202 shall apply to dispositions  
6 in taxable years beginning on or after January 1, 1990.

7 (B) The provisions of Section 10204 shall apply to costs  
8 incurred in taxable years beginning on or after January 1, 1990.

9 (C) Any adjustments required by Section 481 of the Internal  
10 Revenue Code shall be included in gross income as follows:

11 (i) Fifty percent in the first taxable year beginning on or after  
12 January 1, 1990.

13 (ii) Fifty percent in the second taxable year beginning on or  
14 after January 1, 1990.

15 (e) (1) In the case of any installment obligation to which  
16 Section 453A of the Internal Revenue Code applies and which is  
17 outstanding as of the close of the taxable year, in lieu of the  
18 provisions of Section 453A(c)(1) of the Internal Revenue Code,  
19 the tax imposed by Section 17041 or 17048 for the taxable year  
20 shall be increased by the amount of interest determined in the  
21 manner provided under Section 453A(c)(2) of the Internal  
22 Revenue Code.

23 (2) The provisions of Section 453A(c)(3)(B) of the Internal  
24 Revenue Code, relating to the maximum rate used in calculating  
25 the deferred tax liability, are modified to refer to the maximum rate  
26 of tax imposed under Section 17041 in lieu of the maximum rate  
27 of tax imposed under Section 1 or 11 of the Internal Revenue Code.

28 (f) (1) *The last sentence in Section 453A(d)(4) of the Internal*  
29 *Revenue Code, relating to secured indebtedness, shall not apply.*

30 (2) *This subdivision shall apply to sales or other dispositions*  
31 *occurring on or after January 1, 2002.*

32 SEC. 22. *Section 17563.5 is added to the Revenue and*  
33 *Taxation Code, to read:*

34 *17563.5. (a) The amendment by Section 7001(a) of the*  
35 *Internal Revenue Service Restructuring and Reform Act of 1998*  
36 *(Public Law 105-206) to Section 404(a)(11) of the Internal*  
37 *Revenue Code, regarding determinations relating to deferred*  
38 *compensation, shall apply to taxable years beginning on or after*  
39 *January 1, 2002.*

1     **(b)** *In the case of any taxpayer required by the enactment of this*  
2 *section to change its method of accounting for its first taxable year*  
3 *beginning on or after January 1, 2002, each of the following shall*  
4 *apply for purposes of this part, Part 10.2 (commencing with*  
5 *Section 18401), and Part 11 (commencing with Section 23001):*

6     **(1)** *The change shall be treated as initiated by the taxpayer.*

7     **(2)** *The change shall be treated as made with the consent of the*  
8 *Franchise Tax board.*

9     **(3)** *The net amount of the adjustments required to be taken into*  
10 *account by the taxpayer under Chapter 6 (commencing with*  
11 *Section 17551) shall be taken into account ratably over the*  
12 *three-taxable-year period beginning with the taxpayer's first*  
13 *taxable year beginning on or after January 1, 2002.*

14     **SEC. 23.** *Section 17570 of the Revenue and Taxation Code is*  
15 *amended to read:*

16     17570. ~~(a) For each taxable year beginning on or after~~  
17 ~~January 1, 1997, Section 475 of the Internal Revenue Code,~~  
18 ~~relating to mark to market accounting method for securities~~  
19 ~~dealers, shall apply, except as otherwise provided.~~

20     ~~(b)~~ Section 13233(c)(2)(C) of the Revenue Reconciliation Act  
21 of 1993 (P.L. 103-66), relating to the effective date for changes in  
22 the mark to market accounting method for securities dealers, is  
23 modified to provide that the amount taken into account under  
24 Section 481 of the Internal Revenue Code of 1986 shall be taken  
25 into account ratably over the five-taxable-year period beginning  
26 with the first taxable year beginning on or after January 1, 1997.

27     **(b)** *In the case of any taxpayer required by the enactment of the*  
28 *act amending this subdivision, which act incorporated by*  
29 *reference the amendments made by Section 7003 of the Internal*  
30 *Revenue Service Restructuring and Reform Act of 1998 (P.L.*  
31 *105-206) to Section 475 of the Internal Revenue Code for taxable*  
32 *years beginning on or after January 1, 2002, to change its method*  
33 *of accounting for its first taxable year beginning on or after*  
34 *January 1, 2002, then each of the following shall apply for*  
35 *purposes of this part, Part 10.2 (commencing with Section 18401),*  
36 *and Part 11 (commencing with Section 23001):*

37     **(1)** *The change shall be treated as initiated by the taxpayer.*

38     **(2)** *The change shall be treated as made with the consent of the*  
39 *Franchise Tax Board.*

1     (3) *The taxpayer shall not be required to change its method of*  
2 *accounting until its first taxable year beginning on or after*  
3 *January 1, 2002.*

4     (4) *The net amount of the adjustments required to be taken into*  
5 *account by the taxpayer under Chapter 6 (commencing with*  
6 *Section 17551) shall be taken into account ratably over the*  
7 *three-taxable-year period beginning with the taxpayer's first*  
8 *taxable year beginning on or after January 1, 2002.*

9     (c) (1) If a taxpayer has, at any time, made an election for  
10 federal purposes under Section 475(e) of the Internal Revenue  
11 Code, relating to election of mark to market for dealers in  
12 commodities, to have Section 475 of the Internal Revenue Code  
13 apply, Section 475 of the Internal Revenue Code shall apply to that  
14 dealer in commodities for state purposes, a separate election for  
15 state purposes shall not be allowed under paragraph (3) of  
16 subdivision (e) of Section 17024.5, and the federal election shall  
17 be binding for purposes of this part.

18     (2) If a taxpayer fails to make, or has not previously made, an  
19 election for federal purposes under Section 475(e) of the Internal  
20 Revenue Code, relating to election of mark to market for dealers  
21 in commodities, to have Section 475 of the Internal Revenue Code  
22 apply, an election under Section 475(e) of the Internal Revenue  
23 Code shall not be allowed for state purposes, Section 475 of the  
24 Internal Revenue Code shall not apply to that dealer in  
25 commodities for state purposes, and a separate election for state  
26 purposes shall not be allowed under paragraph (3) of subdivision  
27 (e) of Section 17024.5.

28     (d) (1) If a taxpayer has, at any time, made an election for  
29 federal purposes under Section 475(f)(1) of the Internal Revenue  
30 Code, relating to election of mark to market for traders in  
31 securities, to have Section 475 of the Internal Revenue Code apply  
32 to a trade or business, Section 475 of the Internal Revenue Code  
33 shall apply to that trader in securities for state purposes with  
34 respect to that trade or business, a separate election for state  
35 purposes with respect to that trade or business shall not be allowed  
36 under paragraph (3) of subdivision (e) of Section 17024.5, and the  
37 federal election shall be binding for purposes of this part.

38     (2) If a taxpayer fails to make, or has not previously made, an  
39 election for federal purposes under Section 475(f)(1) of the  
40 Internal Revenue Code, relating to election of mark to market for

traders in securities, to have Section 475 of the Internal Revenue Code apply to a trade or business, an election under Section 475(f)(1) of the Internal Revenue Code shall not be allowed for state purposes with respect to that trade or business, Section 475 of the Internal Revenue Code shall not apply to that trader in securities for state purposes with respect to that trade or business, and a separate election for state purposes shall not be allowed under paragraph (3) of subdivision (e) of Section 17024.5.

(e) (1) If a taxpayer has, at any time, made an election for federal purposes under Section 475(f)(2) of the Internal Revenue Code, relating to election of mark to market for traders in commodities, to have Section 475 of the Internal Revenue Code apply to a trade or business, Section 475 of the Internal Revenue Code shall apply to that trader in commodities for state purposes with respect to that trade or business, a separate election for state purposes with respect to that trade or business shall not be allowed under paragraph (3) of subdivision (e) of Section 17024.5, and the federal election with respect to that trade or business shall be binding for purposes of this part.

(2) If a taxpayer fails to make, or has not previously made, an election for federal purposes under Section 475(f)(2) of the Internal Revenue Code, relating to election of mark to market for traders in commodities, to have Section 475 of the Internal Revenue Code apply to a trade or business, an election under Section 475(f)(2) of the Internal Revenue Code shall not be allowed for state purposes with respect to that trade or business, Section 475 of the Internal Revenue Code shall not apply to that trader in commodities for state purposes with respect to that trade or business, and a separate election for state purposes with respect to that trade or business shall not be allowed under paragraph (3) of subdivision (e) of Section 17024.5.

(f) (1) An election under Section 475(e) or (f) of the Internal Revenue Code made for federal purposes with respect to a taxable year beginning before January 1, 1998, shall be treated as having been made for state purposes with respect to the first taxable year beginning on or after January 1, 1998.

(2) Section 1001(d)(4)(B) of the Taxpayer Relief Act of 1997 (P.L. 105-34), relating to the effective date for election of mark to market by securities traders and traders and dealers in commodities, is modified to provide that the requirement for



timely identification shall be treated as timely made for state purposes if that identification is treated as timely made for federal purposes, and the amount taken into account under Section 481 of the Internal Revenue Code of 1986 shall be taken into account ratably over the four-taxable-year period beginning with the first taxable year beginning on or after January 1, 1998.

*SEC. 24. Section 17731.5 of the Revenue and Taxation Code is amended to read:*

17731.5. (a) Section ~~641(d)(2)(A)~~ 641(c)(2)(A) of the Internal Revenue Code is modified to read: “The amount of the tax imposed by subdivision (e) of Section 17041 shall be determined by using the highest rate of tax applicable to an individual under subdivision (a) of Section 17041.”

(b) Section ~~641(d)(2)(B)~~ 641(c)(2)(B) of the Internal Revenue Code is modified to read: “The credit allowed under subdivision (b) of Section 17733 shall be zero.”

*SEC. 25. Section 17751 of the Revenue and Taxation Code is amended to read:*

17751. Section ~~646~~ 645 of the Internal Revenue Code, relating to certain revocable trusts treated as part of estate, is modified as follows:

(a) An election under Section ~~646(a)~~ 645(a) of the Internal Revenue Code for federal purposes shall be treated for purposes of this part as an election made by the executor, if any, of the estate and the trustee of the qualified revocable trust under Section ~~646(a)~~ 645(a) of the Internal Revenue Code for state purposes and a separate election under paragraph (3) of subdivision (e) of Section 17024.5 shall not be allowed.

(b) If the executor, if any, of the estate and the trustee of a qualified revocable trust fail to make an election under Section ~~646(a)~~ 645(a) of the Internal Revenue Code for federal purposes with respect to that qualified revocable trust, that trust shall be treated and taxed for purposes of this part as a separate trust, an election under Section ~~646(a)~~ 645(a) of the Internal Revenue Code for state purposes with respect to that trust shall not be allowed, and a separate election under paragraph (3) of subdivision (e) of Section 17024.5 shall not be allowed with respect to that trust.

*SEC. 26. Section 18038.5 of the Revenue and Taxation Code is amended to read:*



1 18038.5. (a) In the case of any sale of qualified small  
2 business stock held by ~~an individual~~ *a taxpayer other than a*  
3 *corporation* for more than six months and with respect to which  
4 that ~~individual taxpayer~~ elects the application of this section, gain  
5 from that sale shall be recognized only to the extent that the amount  
6 realized on that sale exceeds:

7 (1) The cost of any qualified small business stock purchased by  
8 the taxpayer during the 60-day period beginning on the date of that  
9 sale, reduced by

10 (2) Any portion of the cost previously taken into account under  
11 this section.

12 This section shall not apply to any gain which is treated as  
13 ordinary income for purposes of this part.

14 (b) For purposes of this section:

15 (1) The term “qualified small business stock” has the meaning  
16 given that term by subdivision (c) of Section 18152.5.

17 (2) A taxpayer shall be treated as having purchased any  
18 property if, but for paragraph (3), the unadjusted basis of that  
19 property in the hands of the taxpayer would be its cost (within the  
20 meaning of Section 1012 of the Internal Revenue Code).

21 (3) If gain from any sale is not recognized by reason of  
22 subdivision (a), that gain shall be applied to reduce (in the order  
23 acquired) the basis for determining gain or loss of any qualified  
24 small business stock which is purchased by the taxpayer during the  
25 60-day period described in subdivision (a).

26 (4) For purposes of determining whether the nonrecognition of  
27 gain under subdivision (a) applies to stock which is sold, both of  
28 the following shall apply:

29 (A) The taxpayer’s holding period for that stock and the stock  
30 referred to in paragraph (1) of subdivision (a) shall be determined  
31 without regard to section 1223 of the Internal Revenue Code.

32 (B) Only the first six months of the taxpayer’s holding period  
33 for the stock referred to in paragraph (1) of subdivision (a) shall  
34 be taken into account for purposes of applying paragraph (2) of  
35 subdivision (c) of Section 18152.5.

36 (5) *Rules similar to the rules of subdivisions (f) to (k), inclusive,*  
37 *of Section 18152.5 shall apply.*

38 (c) This section shall apply to sales made after August 5, 1997.

39 SEC. 27. Section 19136 of the Revenue and Taxation Code is  
40 amended to read:

19136. (a) Section 6654 of the Internal Revenue Code, relating to failure by an individual to pay estimated income tax, shall apply, except as otherwise provided.

(b) Section 6654(a)(1) of the Internal Revenue Code is modified to refer to the rate determined under Section 19521 in lieu of Section 6621 of the Internal Revenue Code.

(c) (1) Section 6654(e)(1) of the Internal Revenue Code, relating to exceptions where the tax is a small amount, shall not apply.

(2) No addition to the tax shall be imposed under this section if the tax imposed under Section 17041 or 17048 for the preceding taxable year, minus the sum of any credits against the tax provided by Part 10 (commencing with Section 17001) or this part, or the tax computed under Section 17041 or 17048 upon the estimated income for the taxable year, minus the sum of any credits against the tax provided by Part 10 (commencing with Section 17001) or this part, is less than two hundred dollars (\$200), except in the case of a separate return filed by a married person the amount shall be less than one hundred dollars (\$100).

(d) Section 6654(f) of the Internal Revenue Code shall not apply and for purposes of this section the term “tax” means the tax imposed under Section 17041 or 17048, less any credits against the tax provided by Part 10 (commencing with Section 17001) or this part, other than the credit provided by subdivision (a) of Section 19002.

(e) The credit for tax withheld on wages, as specified in Section 6654(g) of the Internal Revenue Code, shall be the credit allowed under subdivision (a) of Section 19002.

(f) This section shall apply to a nonresident individual.

~~SEC. 23.~~

SEC. 28. Section 19136.8 is added to the Revenue and Taxation Code, to read:

19136.8. (a) No addition to tax shall be made under Section 19136 for any period before April 15, 2003, with respect to any underpayment of an installment for the 2002 taxable year, to the extent that the underpayment was created or increased by any provision of the act adding this section.

(b) No addition of tax shall be made under Section 19142 for any period before April 15, 2003, with respect to any underpayment of an installment for the 2002 taxable year, to the

1 extent that the underpayment was created or increased by any  
2 provision of the act adding this section.

3 (c) The Franchise Tax Board shall implement this section in a  
4 reasonable manner.

5 ~~SEC. 24.~~

6 *SEC. 29. Section 19141 of the Revenue and Taxation Code is*  
7 *amended to read:*

8 19141. Upon certification by the Secretary of State pursuant  
9 to subdivision (a) of Section 2204 *or subdivision (a) of Section*  
10 *17563* of the Corporations Code, the Franchise Tax Board shall  
11 assess a penalty of two hundred fifty dollars (\$250). Upon  
12 certification by the Secretary of State pursuant to subdivision (a)  
13 of Section 6810 or subdivision (a) of Section 8810 of the  
14 Corporations Code, the Franchise Tax Board shall assess a penalty  
15 of fifty dollars (\$50). Any such penalty shall be a final assessment  
16 due and payable at the time of assessment but no interest shall  
17 accrue thereon. The assessment shall be collected as other taxes,  
18 interest, and penalties are collected by the Franchise Tax Board  
19 unless the Secretary of State decertifies the name of the  
20 corporation as provided in subdivision (e) or (f) of Section 2204,  
21 subdivision (e) of Section 6810, or subdivision (e) of Section 8810  
22 of the Corporations Code.

23 *SEC. 30. Section 19365 of the Revenue and Taxation Code is*  
24 *amended to read:*

25 19365. (a) (1) A corporation that is treated as an “S  
26 corporation” for a taxable year beginning in 2002 under Chapter  
27 4.5 (commencing with Section 23800) of Part 11 may file an  
28 application for the transfer of an overpayment with respect to  
29 payments of estimated tax for taxable years beginning in 2002 to  
30 the personal income tax accounts of its shareholders. An  
31 application under this subdivision shall not constitute a claim for  
32 credit or refund.

33 (2) An application under this subdivision shall be verified in  
34 the manner prescribed by Section 18621 in the case of the  
35 taxpayer, and shall be filed in the manner and form prescribed by  
36 the Franchise Tax Board. The application shall set forth all of the  
37 following:

38 (A) The amount the “S corporation” estimates as its tax  
39 liability under this part for the taxable year, which shall not be less

1 than the greater of  $1\frac{1}{2}$  percent of its net income or the applicable  
2 minimum franchise tax.

3 (B) The amount and date of the estimated tax paid during the  
4 taxable year.

5 (C) For each shareholder affected, his or her name, social  
6 security account number, address, and percentage of ownership,  
7 and any changes in that percentage of ownership for the S  
8 corporation's taxable year, the amount of each overpayment to be  
9 transferred, and the date the amount was paid.

10 (D) Any other information for purposes of carrying out this  
11 section as may be required by the Franchise Tax Board.

12 (b) (1) Within a period of 45 days from the date on which an  
13 application for a transfer is filed under subdivision (a), the  
14 Franchise Tax Board shall make, to the extent it deems practicable  
15 in that period, a limited examination of the application to discover  
16 omissions and errors therein, and shall determine the final amount  
17 of the transfers upon the basis of the application and the  
18 examination, except that the Franchise Tax Board may disallow,  
19 without further action, any application which it finds contains  
20 material omissions or errors which it deems cannot be corrected  
21 within the 45-day period.

22 (2) The Franchise Tax Board, within the 45-day period referred  
23 to in paragraph (1), may credit the amount of the overpayment  
24 against any liability on the part of the taxpayer under Part 11  
25 (commencing with Section 23001).

26 (3) In the event the amount available for transfer is less than  
27 requested by the taxpayer, the overpayment amount shall be  
28 allocated among the shareholders on a pro rata basis based on their  
29 percentage of ownership stated on the application.

30 (4) For purposes of Part 10 (commencing with Section 17001),  
31 Part 11 (commencing with Section 23001), and this part, the  
32 transferred amounts shall be treated as if they had been estimated  
33 tax payments paid by the respective shareholders on the date  
34 originally paid by the corporation.

35 (5) No application under subdivision (a) shall be allowed  
36 unless the amount to be transferred equals or exceeds five hundred  
37 dollars (\$500).

38 (6) Each S corporation which files an application for transfer  
39 of overpayments under subdivision (a) shall furnish to each person  
40 who is a shareholder at any time during the taxable year a statement

1 showing amounts and dates of the overpayments being transferred  
2 to that person's personal income tax account.

3 ~~SEC. 25. Section 23038.5 of the Revenue and Taxation Code~~  
4 ~~is amended to read:~~

5 ~~23038.5. (a) Section 7704 of the Internal Revenue Code,~~  
6 ~~relating to certain publicly traded partnerships treated as~~  
7 ~~corporations, shall apply, except as otherwise provided.~~

8 ~~(b) (1) Section 7704(a) of the Internal Revenue Code shall not~~  
9 ~~apply to an electing 1987 partnership.~~

10 ~~(2) For purposes of this subdivision, the term "electing 1987~~  
11 ~~partnership" means any publicly traded partnership if all of the~~  
12 ~~following apply:~~

13 ~~(A) The partnership is an existing partnership (as defined in~~  
14 ~~Section 10211(c)(2) of the Revenue Reconciliation Act of 1987).~~

15 ~~(B) Section 7704(a) of the Internal Revenue Code has not~~  
16 ~~applied (and without regard to Section 7704(c)(1) of the Internal~~  
17 ~~Revenue Code would not have applied) to that partnership for all~~  
18 ~~prior taxable years beginning after December 31, 1987, and before~~  
19 ~~January 1, 1998.~~

20 ~~(C) (i) The partnership has made the election under Section~~  
21 ~~7704(g)(1)(C) of the Internal Revenue Code (as added by Public~~  
22 ~~Law 105-34) for federal income tax purposes.~~

23 ~~(ii) The election for federal income tax purposes described in~~  
24 ~~clause (i) shall be treated as a binding election and a separate~~  
25 ~~election for state tax purposes shall not be allowed.~~

26 ~~(iii) The election for federal income tax purposes described in~~  
27 ~~clause (i) shall be treated as a binding consent to the application of~~  
28 ~~the tax imposed under paragraph (3) and a separate election for~~  
29 ~~state tax purposes shall not be allowed.~~

30 ~~(D) A partnership which, but for this subparagraph, would be~~  
31 ~~treated as an electing 1987 partnership shall cease to be so treated~~  
32 ~~(and the election under subparagraph (C) shall cease to be in effect)~~  
33 ~~as of the first day after December 31, 1997, that the partnership is~~  
34 ~~no longer treated as an electing 1987 partnership for federal tax~~  
35 ~~purposes (and the election under Section 7704(g)(1)(C) of the~~  
36 ~~Internal Revenue Code (as added by Public Law 105-34) ceases to~~  
37 ~~be in effect for federal income tax purposes).~~

38 ~~(3) (A) There is hereby imposed for each taxable year~~  
39 ~~beginning on or after January 1, 1998, on the gross income of each~~  
40 ~~electing 1987 partnership a tax equal to 1 percent of that~~

1 partnership's gross income from all sources reportable to this state,  
2 taking into account Section 25101 and any election under Section  
3 25110, attributable to the active conduct of trades and businesses  
4 by the partnership.

5 (B) The tax shall be due and payable on the date the return of  
6 the partnership is required to be filed under Section 18633, shall  
7 be collected and refunded in the same manner as other taxes  
8 imposed by this part, and shall be subject to interest and applicable  
9 penalties.

10 (C) For purposes of this paragraph, if a partnership is a partner  
11 in another partnership, the gross income referred to in  
12 subparagraph (A) shall include the partnership's distributive share  
13 of the gross income of the other partnership from all sources  
14 reportable to this state, taking into account Section 25101 and any  
15 election under Section 25110, attributable to the active conduct of  
16 trades and businesses of that other partnership. A similar rule shall  
17 apply in the case of lower-tiered partnerships.

18 (D) The tax imposed by this paragraph shall be treated as  
19 imposed by this part other than for purposes of determining the  
20 amount of any credit allowable under this part.

21 (4) The provisions of this subdivision shall apply to the taxable  
22 year for which the election described in clause (i) of subparagraph  
23 (C) of paragraph (2) is made for federal income tax purposes and  
24 all subsequent taxable years unless revoked by the partnership for  
25 federal income tax purposes. Any revocation made for federal  
26 income tax purposes shall be treated as a binding revocation under  
27 this part, but, once so revoked, may not be reinstated and a separate  
28 revocation for state purposes shall not be allowed.

29 (e) The amendment made to this section by the act adding this  
30 subdivision shall apply to taxable years beginning on or after  
31 January 1, 1998.

32 SEC. 26.—Section 23051.5 of the Revenue and Taxation Code  
33 is amended to read:

34 23051.5.—(a) (1) Unless otherwise specifically provided, the  
35 terms “Internal Revenue Code,” “Internal Revenue Code of  
36 1954,” or “Internal Revenue Code of 1986,” for purposes of this  
37 part, mean Title 26 of the United States Code, including all  
38 amendments thereto, as enacted on the specified date for the  
39 applicable taxable year as defined in paragraph (1) of subdivision  
40 (a) of Section 17024.5.

~~(2) Unless otherwise specifically provided, for federal laws enacted on or after January 1, 1987, and on or before the specified date for the taxable year, uncodified provisions that relate to provisions of the Internal Revenue Code that are incorporated for purposes of this part, shall be applicable to the same taxable years as the incorporated provisions.~~

~~(3) Subtitle G (Tax Technical Corrections) and Part I of Subtitle H (Repeal of Expired or Obsolete Provisions) of the Revenue Reconciliation Act of 1990 (Public Law 101-508) modified numerous provisions of the Internal Revenue Code and provisions of prior federal acts, some of which are incorporated by reference into this part. Unless otherwise provided, the provisions described in the preceding sentence, to the extent that they modify provisions that are incorporated into this part, are declaratory of existing law and shall be applied in the same manner and for the same periods as specified in the Revenue Reconciliation Act of 1990.~~

~~(b) Unless otherwise specifically provided, when applying the Internal Revenue Code for purposes of this part, a reference to any of the following shall not be applicable for purposes of this part:~~

~~(1) Domestic International Sales Corporations (DISC), as defined in Section 992(a) of the Internal Revenue Code.~~

~~(2) Foreign Sales Corporations (FSC), as defined in Section 922(a) of the Internal Revenue Code.~~

~~(3) A personal holding company, as defined in Section 542 of the Internal Revenue Code.~~

~~(4) A foreign personal holding company, as defined in Section 552 of the Internal Revenue Code.~~

~~(5) A foreign investment company, as defined in Section 1246(b) of the Internal Revenue Code.~~

~~(6) A foreign trust as defined in Section 679 of the Internal Revenue Code.~~

~~(7) Foreign income taxes and foreign income tax credits.~~

~~(8) Federal tax credits and carryovers of federal tax credits.~~

~~(c) (1) The provisions contained in Sections 41 to 44, inclusive, and Section 172 of the Tax Reform Act of 1984 (Public Law 98-369), relating to treatment of debt instruments, shall not be applicable for taxable years beginning before January 1, 1987.~~

~~(2) The provisions contained in Public Law 99-121, relating to the treatment of debt instruments, shall not be applicable for taxable years beginning before January 1, 1987.~~



1 ~~(3) For taxable years beginning on and after January 1, 1987,~~  
2 ~~the provisions referred to by paragraphs (1) and (2) shall be~~  
3 ~~applicable for purposes of this part in the same manner and with~~  
4 ~~respect to the same obligations as the federal provisions, except as~~  
5 ~~otherwise provided in this part.~~

6 ~~(d) When applying the Internal Revenue Code for purposes of~~  
7 ~~this part, regulations promulgated in final form or issued as~~  
8 ~~temporary regulations by “the secretary” shall be applicable as~~  
9 ~~regulations issued under this part to the extent that they do not~~  
10 ~~conflict with this part or with regulations issued by the Franchise~~  
11 ~~Tax Board.~~

12 ~~(e) Whenever this part allows a taxpayer to make an election on~~  
13 ~~or after January 1, 2002, in taxable years beginning on or after~~  
14 ~~January 1, 2002, the following rules shall apply:~~

15 ~~(1) A proper election for federal income tax purposes filed with~~  
16 ~~the Internal Revenue Service in accordance with the Internal~~  
17 ~~Revenue Code or regulations issued by “the secretary” shall~~  
18 ~~treated as an election for purposes of this part and a separate~~  
19 ~~election for state purposes shall not be allowed, unless otherwise~~  
20 ~~expressly provided in this part or in regulations issued by the~~  
21 ~~Franchise Tax Board.~~

22 ~~(2) A copy of that election shall be furnished to the Franchise~~  
23 ~~Tax Board upon request.~~

24 ~~(3) If the taxpayer does not make a proper election for federal~~  
25 ~~income tax purposes a separate election for purposes of this part~~  
26 ~~shall not be allowed, unless otherwise provided.~~

27 ~~(f) Whenever this part allows or requires a taxpayer to file an~~  
28 ~~application or seek consent, the rules set forth in subdivision (e)~~  
29 ~~shall apply to that application or consent.~~

30 ~~(g) When applying the Internal Revenue Code for purposes of~~  
31 ~~determining the statute of limitations under this part, any reference~~  
32 ~~to a period of three years shall be modified to read four years for~~  
33 ~~purposes of this part.~~

34 ~~(h) When applying, for purposes of this part, any section of the~~  
35 ~~Internal Revenue Code or any applicable regulation thereunder, all~~  
36 ~~of the following shall apply:~~

37 ~~(1) For purposes of Chapter 2 (commencing with Section~~  
38 ~~23101), Chapter 2.5 (commencing with Section 23400), and~~  
39 ~~Chapter 3 (commencing with Section 23501), the term “taxable~~  
40 ~~income” shall mean “net income.”~~

~~(2) For purposes of Article 2 (commencing with Section 23731) of Chapter 4, the term “taxable income” shall mean “unrelated business taxable income,” as defined by Section 23732.~~

~~(3) Any reference to “subtitle,” “Chapter 1,” or “chapter” shall mean this part.~~

~~(4) The provisions of Section 7806 of the Internal Revenue Code, relating to construction of title, shall apply.~~

~~(5) Any provision of the Internal Revenue Code that becomes operative on or after the specified date for that taxable year shall become operative on the same date for purposes of this part.~~

~~(6) Any provision of the Internal Revenue Code that becomes inoperative on or after the specified date for that taxable year shall become inoperative on the same date for purposes of this part.~~

~~(7) Due account shall be made for differences in federal and state terminology, effective dates, substitution of “Franchise Tax Board” for “secretary” when appropriate, and other obvious differences.~~

~~(8) Any provision of the Internal Revenue Code that refers to a “corporation” shall, when applicable for purposes of this part, include a “bank,” as defined by Section 23039.~~

~~(i) Any reference to a specific provision of the Internal Revenue Code shall include modifications of that provision, if any, in this part.~~

~~SEC. 27.—~~

~~SEC. 31. Section 19521 of the Revenue and Taxation Code is amended to read:~~

~~19521. (a) The rate established under this section (referred to in other code sections as “the adjusted annual rate”) shall be determined in accordance with Section 6621 of the Internal Revenue Code, except that:~~

~~(1) The overpayment rate specified in Section 6621(a)(1) of the Internal Revenue Code shall be modified to be equal to the underpayment rate determined under Section 6621(a)(2) of the Internal Revenue Code; and~~

~~(2) The determination specified in Section 6621(b) of the Internal Revenue Code shall be modified to be determined semiannually as follows:~~

~~(A) The rate for January shall apply during the following July through December, and~~

(B) The rate for July shall apply during the following January through June.

(b) (1) For purposes of this part, Part 10 (commencing with Section 17001), Part 11 (commencing with Section 23001), and any other provision of law referencing this method of computation, in computing the amount of any interest required to be paid by the state or by the taxpayer, or any other amount determined by reference to that amount of interest, that interest and that amount shall be compounded daily.

(2) Paragraph (1) shall not apply for purposes of computing the amount of any addition to tax under Section 19136 or 19142.

(c) Section 6621(c) of the Internal Revenue Code, relating to increase in underpayment rate for large corporate underpayments, is modified as follows:

(1) The applicable date shall be the 30th day after the earlier of either of the following:

(A) The date on which the proposed deficiency assessment is issued.

(B) The date on which the notice and demand is sent.

(2) This subdivision shall apply for purposes of determining interest for periods after December 31, 1991.

(3) Section 6621(c)(2)(B)(iii) of the Internal Revenue Code shall apply for purposes of determining interest for periods after December 31, 1998.

*(d) Section 6621(d) of the Internal Revenue Code, relating to elimination of interest on overlapping periods of tax overpayments and underpayments, shall not apply.*

*SEC. 32. Section 23038.5 of the Revenue and Taxation Code is amended to read:*

23038.5. (a) Section 7704 of the Internal Revenue Code, relating to certain publicly traded partnerships treated as corporations, shall apply, except as otherwise provided.

(b) (1) Section 7704(a) of the Internal Revenue Code shall not apply to an electing 1987 partnership.

(2) For purposes of this subdivision, the term “electing 1987 partnership” means any publicly traded partnership if all of the following apply:

(A) The partnership is an existing partnership (as defined in Section 10211(c)(2) of the Revenue Reconciliation Act of 1987).

(B) Section 7704(a) of the Internal Revenue Code has not applied (and without regard to Section 7704(c)(1) of the Internal Revenue Code would not have applied) to that partnership for all prior taxable years beginning after December 31, 1987, and before January 1, 1998.

(C) (i) The partnership has made the election under Section ~~7704(g)(1)(C)~~ 7704(g)(2)(C) of the Internal Revenue Code ~~(as added by Public Law 105-34)~~ for federal tax purposes.

(ii) The election for federal tax purposes described in clause (i) shall be treated as a binding election and a separate election for state tax purposes shall not be allowed under paragraph (3) of subdivision (e) of Section 23051.5.

(iii) The election for federal tax purposes described in clause (i) shall be treated as a binding consent to the application of the tax imposed under paragraph (3) and a separate election for state tax purposes shall not be allowed under paragraph (3) of subdivision (e) of Section 23051.5.

(D) A partnership which, but for this subparagraph, would be treated as an electing 1987 partnership shall cease to be so treated (and the election under subparagraph (C) shall cease to be in effect) as of the first day after December 31, 1997, that the partnership is no longer treated as an electing 1987 partnership for federal tax purposes (and the election under Section ~~7704(g)(1)(C)~~ 7704(g)(2)(C) of the Internal Revenue Code ~~(as added by Public Law 105-34)~~ ceases to be in effect for federal tax purposes).

(3) (A) There is hereby imposed for each taxable year beginning on or after January 1, 1998, on the gross income of each electing 1987 partnership a tax equal to 1 percent of that partnership's gross income from all sources reportable to this state, taking into account Section 25101 and any election under Section 25110, attributable to the active conduct of trades and businesses by the partnership.

(B) The tax shall be due and payable on the date the return of the partnership is required to be filed under Section ~~48633~~, 18633 *and shall be paid by the partnership. The tax shall be paid, collected, and refunded in the same manner as other taxes imposed by this part on corporations, and shall be subject to interest and applicable penalties. Section 19147 shall be applied to the partnership with respect to the tax imposed by this paragraph in*

1 *the same manner as if references in that section to taxable income*  
2 *were references to gross income referred to in subparagraph (A).*

3 (C) For purposes of this paragraph, if a partnership is a partner  
4 in another partnership, the gross income referred to in  
5 subparagraph (A) shall include the partnership's distributive share  
6 of the gross income of the other partnership from all sources  
7 reportable to this state, taking into account Section 25101 and any  
8 election under Section 25110, attributable to the active conduct of  
9 trades and businesses of that other partnership. A similar rule shall  
10 apply in the case of lower-tiered partnerships.

11 (D) The tax imposed by this paragraph shall be treated as  
12 imposed by this part other than for purposes of determining the  
13 amount of any credit allowable under this part.

14 (4) The provisions of this subdivision shall apply to the taxable  
15 year for which the election described in clause (i) of subparagraph  
16 (C) of paragraph (2) is made for federal purposes and all  
17 subsequent taxable years unless revoked by the partnership for  
18 federal purposes. Any revocation made for federal purposes shall  
19 be treated as a binding revocation under this part, but, once so  
20 revoked, may not be reinstated and a separate revocation for state  
21 purposes shall not be allowed under paragraph (3) of subdivision  
22 (e) of Section 23051.5.

23 (c) The amendment made to this section by the act adding this  
24 subdivision shall apply to taxable years beginning on or after  
25 January 1, 1998.

26 SEC. 33. Section 23456 of the Revenue and Taxation Code is  
27 amended to read:

28 23456. For purposes of this part, Section 56 of the Internal  
29 Revenue Code is modified as follows:

30 (a) (1) Section 56(a)(2) of the Internal Revenue Code, relating  
31 to mining exploration and development costs, shall apply only to  
32 expenses incurred during taxable years beginning on or after  
33 January 1, 1988.

34 (2) Section 56(a)(5) of the Internal Revenue Code, relating to  
35 pollution control facilities, shall apply only to amounts allowable  
36 as a deduction under Section 24372.3.

37 (3) (A) Section 56(a)(6) of the Internal Revenue Code, as in  
38 effect on January 1, 1997, relating to installment sales of certain  
39 property, shall not apply to payments received in taxable years

beginning on or after January 1, 1997, with respect to dispositions occurring in taxable years beginning after December 31, 1987.

(B) This paragraph shall not apply to any taxable year beginning on or after January 1, 1998.

(b) For purposes of applying Section 56(d) of the Internal Revenue Code, all references to “December 31, 1986,” are modified to read “December 31, 1987,” and all references to “January 1, 1987,” are modified to read “January 1, 1988.”

(c) Section 56(d)(1) of the Internal Revenue Code, relating to the alternative tax net operating loss deduction, is modified to include the provisions of Section 25108.

(d) For each taxable year beginning on or after January 1, 1988, and before January 1, 1990, Section 56(f)(2)(E) of the Internal Revenue Code, as it read during that period, is modified to refer to both of the following:

(1) Cooperatives under Section 24404 in lieu of the deduction allowed under Section 1382(b) of the Internal Revenue Code.

(2) Credit unions under Section 24405 as though the deduction allowed under Section 1382(b) of the Internal Revenue Code applied to credit unions.

(e) Section 56(g) of the Internal Revenue Code, relating to adjustments based on adjusted current earnings, is modified to provide that for corporations whose income is determined under Chapter 17 (commencing with Section 25101), adjusted current earnings shall be allocated and apportioned in the same manner as net income is allocated and apportioned for purposes of the regular tax. In addition, each of the following shall apply:

(1) Sections 56(g)(1)(A) and 56(g)(3) of the Internal Revenue Code are modified to provide that the term “adjusted current earnings” means the sum of the adjusted current earnings of that corporation apportionable to this state and the adjusted current earnings allocable to this state.

(2) Section 56(g)(1)(B) of the Internal Revenue Code is modified to provide that the term “alternative minimum taxable income” means the sum of the alternative minimum taxable income of that corporation apportionable to this state and the alternative minimum taxable income allocable to this state.

(f) Section 56(g)(4)(A) of the Internal Revenue Code is modified to provide the following:

(1) In the case of any property placed in service on or after January 1, 1981, and prior to January 1, 1987, other than residential rental property for which an election was made under former Section 24349.5, the amount allowable as depreciation or amortization with respect to that property shall be the same amount that would have been allowable for the taxable year had the taxpayer depreciated the property under the straight-line method for each taxable year of the useful life (determined without regard to Section 24354.2) for which the taxpayer has held the property.

(2) In the case of any property placed in service on or after January 1, 1987, and prior to January 1, 1990, other than residential rental property for which an election was made under former Section 24349.5, the amount allowable as depreciation or amortization with respect to that property shall be determined by each of the following:

(A) Taking into account the adjusted basis of that property (as determined for purposes of computing alternative minimum taxable income) as of the close of the last taxable year beginning before January 1, 1990.

(B) Using the straight-line method over the remainder of the recovery period applicable to that property under the alternative system of Section 168(g) of the Internal Revenue Code.

(3) The amendments made to paragraph (2) by the act adding this paragraph shall apply to taxable years beginning on or after January 1, 1990.

(4) The last sentence of Section 56(g)(4)(A)(i) of the Internal Revenue Code, shall not apply to taxable years beginning before January 1, 1998.

(g) (1) Section 56(g)(4)(C) of the Internal Revenue Code, relating to disallowance of items not deductible in computing earnings and profits, shall be modified as follows:

(A) (i) A deduction shall be allowed for amounts allowable as a deduction for purposes of the regular tax under Sections 24402, 24410, 24411, and 25106.

(ii) For each taxable year beginning on or after January 1, 1990, a deduction shall be allowed for amounts allowable as a deduction to a credit union for purposes of the regular tax under Section 24405.



(B) Section 56(g)(4)(C)(ii) of the Internal Revenue Code, relating to special rule for 100-percent dividends, shall not be applicable.

(C) Section 56(g)(4)(C)(iii) of the Internal Revenue Code, relating to special rule for dividends from Section 936 companies, shall not be applicable.

(D) Section 56(g)(4)(C)(iv) of the Internal Revenue Code, relating to special rule for certain dividends received by certain cooperatives, shall not be applicable.

(2) Section 56(g)(4)(D)(ii) of the Internal Revenue Code is modified to specify that Sections 24364 and 24407 shall not apply to expenditures paid or incurred in taxable years beginning on or after January 1, 1990.

(3) With respect to corporations which are not subject to the tax imposed under Chapter 2 (commencing with Section 23101), the amount of interest income included in the adjusted current earnings shall not exceed the amount of interest income included for purposes of the regular tax.

(4) Appropriate adjustments shall be made to limit deductions from adjusted current earnings for interest expense in accordance with the provisions of Sections 24344 and 24425.

~~SEC. 28.~~

*SEC. 34. Section 23456.5 is added to the Revenue and Taxation Code, to read:*

*23456.5. The amendments made to Section 56, relating to adjustments in computing alternative minimum taxable income, by Section 4(1) of Public Law 106-519, relating to the exclusion under Section 114 of the Internal Revenue Code, shall not apply.*

*SEC. 35. Section 23457 of the Revenue and Taxation Code is amended to read:*

*23457. For purposes of this part, Section 57 of the Internal Revenue Code is modified as follows:*

(a) Section 57(a)(5) of the Internal Revenue Code, relating to tax-exempt interest, shall not be applicable.

(b) Section 57(a) of the Internal Revenue Code, relating to items of tax preference, is modified to include as an item of tax preference the amount by which the deduction allowable under Section 24348 for the taxable year for a reasonable addition to a reserve for bad debts exceeds the amount that would have been

allowable had the taxpayer maintained its bad debt reserve for all taxable years on the basis of actual experience.

(c) Section 57(a)(6) of the Internal Revenue Code, relating to accelerated depreciation or amortization on certain property placed in service before January 1, 1987, is modified to read: With respect to each property as described in Section 1250(c) of the Internal Revenue Code as that provision read on April 1, 1970, the amount by which the deduction allowable for the taxable year for exhaustion, wear, tear, obsolescence, or amortization exceeds the depreciation deduction which would have been allowable for the taxable year, had the taxpayer depreciated the property under the straight-line method for each taxable year of its useful life (determined without regard to Section 24354.2 or 24381) for which the taxpayer has held the property.

~~SEC. 28.2. — Section 23609 of the Revenue and Taxation Code is amended to read:~~

~~23609. — For each taxable year beginning on or after January 1, 1987, there shall be allowed as a credit against the “tax” (as defined by Section 23036) an amount determined in accordance with Section 41 of the Internal Revenue Code, except as follows:~~

~~(a) For each taxable year beginning before January 1, 1997, both of the following modifications shall apply:~~

~~(1) The reference to “20 percent” in Section 41(a)(1) of the Internal Revenue Code is modified to read “8 percent.”~~

~~(2) The reference to “20 percent” in Section 41(a)(2) of the Internal Revenue Code is modified to read “12 percent.”~~

~~(b) (1) For each taxable year beginning on or after January 1, 1997, and before January 1, 1999, both of the following modifications shall apply:~~

~~(A) The reference to “20 percent” in Section 41(a)(1) of the Internal Revenue Code is modified to read “11 percent.”~~

~~(B) The reference to “20 percent” in Section 41(a)(2) of the Internal Revenue Code is modified to read “24 percent.”~~

~~(2) For each taxable year beginning on or after January 1, 1999, and before January 1, 2000, both of the following shall apply:~~

~~(A) The reference to “20 percent” in Section 41(a)(1) of the Internal Revenue Code is modified to read “12 percent.”~~

~~(B) The reference to “20 percent” in Section 41(a)(2) of the Internal Revenue Code is modified to read “24 percent.”~~

1     ~~(3) For each taxable year beginning on or after January 1, 2000,~~  
2     ~~both of the following shall apply:~~  
3     ~~(A) The reference to “20 percent” in Section 41(a)(1) of the~~  
4     ~~Internal Revenue Code is modified to read “15 percent.”~~  
5     ~~(B) The reference to “20 percent” in Section 41(a)(2) of the~~  
6     ~~Internal Revenue Code is modified to read “24 percent.”~~  
7     ~~(c) (1) With respect to any expense paid or incurred after the~~  
8     ~~operative date of Section 6378, Section 41(b)(1) of the Internal~~  
9     ~~Revenue Code is modified to exclude from the definition of~~  
10    ~~“qualified research expense” any amount paid or incurred for~~  
11    ~~tangible personal property that is eligible for the exemption from~~  
12    ~~sales or use tax provided by Section 6378.~~  
13    ~~(2) “Qualified research” and “basic research” shall include~~  
14    ~~only research conducted in California.~~  
15    ~~(d) The provisions of Section 41(e)(7)(A) of the Internal~~  
16    ~~Revenue Code, shall be modified so that “basic research,” for~~  
17    ~~purposes of this section, includes any basic or applied research~~  
18    ~~including scientific inquiry or original investigation for the~~  
19    ~~advancement of scientific or engineering knowledge or the~~  
20    ~~improved effectiveness of commercial products, except that the~~  
21    ~~term does not include any of the following:~~  
22    ~~(1) Basic research conducted outside California.~~  
23    ~~(2) Basic research in the social sciences, arts, or humanities.~~  
24    ~~(3) Basic research for the purpose of improving a commercial~~  
25    ~~product if the improvements relate to style, taste, cosmetic, or~~  
26    ~~seasonal design factors.~~  
27    ~~(4) Any expenditure paid or incurred for the purpose of~~  
28    ~~ascertaining the existence, location, extent, or quality of any~~  
29    ~~deposit of ore or other mineral (including oil and gas).~~  
30    ~~(e) (1) In the case of a taxpayer engaged in any~~  
31    ~~biopharmaceutical research activities that are described in codes~~  
32    ~~2833 to 2836, inclusive, or any research activities that are~~  
33    ~~described in codes 3826, 3829, or 3841 to 3845, inclusive, of the~~  
34    ~~Standard Industrial Classification (SIC) Manual published by the~~  
35    ~~United States Office of Management and Budget, 1987 edition, or~~  
36    ~~any other biotechnology research and development activities, the~~  
37    ~~provisions of Section 41(e)(6) of the Internal Revenue Code shall~~  
38    ~~be modified to include both of the following:~~  
39    ~~(A) A qualified organization as described in Section~~  
40    ~~170(b)(1)(A)(iii) of the Internal Revenue Code and owned by an~~

1 ~~institution of higher education as described in Section 3304(f) of~~  
2 ~~the Internal Revenue Code.~~

3 ~~(B) A charitable research hospital owned by an organization~~  
4 ~~that is described in Section 501(c)(3) of the Internal Revenue~~  
5 ~~Code, is exempt from taxation under Section 501(a) of the Internal~~  
6 ~~Revenue Code, is not a private foundation, is designated a~~  
7 ~~“specialized laboratory cancer center,” and has received Clinical~~  
8 ~~Cancer Research Center status from the National Cancer Institute.~~

9 ~~(2) For purposes of this subdivision:~~

10 ~~(A) “Biopharmaceutical research activities” means those~~  
11 ~~activities that use organisms or materials derived from organisms,~~  
12 ~~and their cellular, subcellular, or molecular components, in order~~  
13 ~~to provide pharmaceutical products for human or animal~~  
14 ~~therapeutics and diagnostics. Biopharmaceutical activities make~~  
15 ~~use of living organisms to make commercial products, as opposed~~  
16 ~~to pharmaceutical activities that make use of chemical compounds~~  
17 ~~to produce commercial products.~~

18 ~~(B) “Other biotechnology research and development~~  
19 ~~activities” means research and development activities consisting~~  
20 ~~of the application of recombinant DNA technology to produce~~  
21 ~~commercial products, as well as research and development~~  
22 ~~activities regarding pharmaceutical delivery systems designed to~~  
23 ~~provide a measure of control over the rate, duration, and site of~~  
24 ~~pharmaceutical delivery.~~

25 ~~(f) In the case where the credit allowed by this section exceeds~~  
26 ~~the “tax,” the excess may be carried over to reduce the “tax” in~~  
27 ~~the following year, and succeeding years if necessary, until the~~  
28 ~~credit has been exhausted.~~

29 ~~(g) For each taxable year beginning on or after January 1, 1998,~~  
30 ~~the reference to “Section 501(a)” in Section 41(b)(3)(C) of the~~  
31 ~~Internal Revenue Code, relating to contract research expenses, is~~  
32 ~~modified to read “this part of Part 10 (commencing with Section~~  
33 ~~17001).”~~

34 ~~(h) (1) For each taxable year beginning on or after January 1,~~  
35 ~~1998, and before January 1, 2000:~~

36 ~~(A) The reference to “1.65 percent” in Section 41(c)(4)(A)(i)~~  
37 ~~of the Internal Revenue Code is modified to read “one and~~  
38 ~~thirty-two hundredths of one percent.”~~

~~(B) The reference to “2.2 percent” in Section 41(c)(4)(A)(ii) of the Internal Revenue Code is modified to read “one and seventy-six hundredths of one percent.”~~

~~(C) The reference to “2.75 percent” in Section 41(c)(4)(A)(iii) of the Internal Revenue Code is modified to read “two and two-tenths of one percent.”~~

~~(2) For each taxable year beginning on or after January 1, 2000:~~

~~(A) The reference to “1.65 percent” in Section 41(c)(4)(A)(i) of the Internal Revenue Code is modified to read “one and forty-nine hundredths of one percent.”~~

~~(B) The reference to “2.2 percent” in Section 41(c)(4)(A)(ii) of the Internal Revenue Code is modified to read “one and ninety-eight hundredths of one percent.”~~

~~(C) The reference to “2.75 percent” in Section 41(c)(4)(A)(iii) of the Internal Revenue Code is modified to read “two and forty-eight hundredths of one percent.”~~

~~(3) Section 41(e)(6) of the Internal Revenue Code, relating to gross receipts, is modified to take into account only those gross receipts from the sale of property held primarily for sale to customers in the ordinary course of the taxpayer’s trade or business that is delivered or shipped to a purchaser within this state, regardless of f.o.b. point or any other condition of the sale.~~

~~(i) Section 41(h) of the Internal Revenue Code, relating to termination, shall not apply.~~

~~(j) Section 41(g) of the Internal Revenue Code, relating to special rule for passthrough of credit, is modified by each of the following:~~

~~(1) The last sentence shall not apply.~~

~~(2) If the amount determined under Section 41(a) of the Internal Revenue Code for any taxable year exceeds the limitation of Section 41(g) of the Internal Revenue Code, that amount may be carried over to other taxable years under the rules of subdivision (f), except that the limitation of Section 41(g) of the Internal Revenue Code shall be taken into account in each subsequent taxable year.~~

~~SEC. 29.—~~

*SEC. 36. Section 23609 of the Revenue and Taxation Code is amended to read:*

23609. For each taxable year beginning on or after January 1, 1987, there shall be allowed as a credit against the “tax” (as

defined by Section 23036) an amount determined in accordance with Section 41 of the Internal Revenue Code, except as follows:

(a) For each taxable year beginning before January 1, 1997, both of the following modifications shall apply:

(1) The reference to “20 percent” in Section 41(a)(1) of the Internal Revenue Code is modified to read “8 percent.”

(2) The reference to “20 percent” in Section 41(a)(2) of the Internal Revenue Code is modified to read “12 percent.”

(b) (1) For each taxable year beginning on or after January 1, 1997, and before January 1, 1999, both of the following modifications shall apply:

(A) The reference to “20 percent” in Section 41(a)(1) of the Internal Revenue Code is modified to read “11 percent.”

(B) The reference to “20 percent” in Section 41(a)(2) of the Internal Revenue Code is modified to read “24 percent.”

(2) For each taxable year beginning on or after January 1, 1999, and before January 1, 2000, both of the following shall apply:

(A) The reference to “20 percent” in Section 41(a)(1) of the Internal Revenue Code is modified to read “12 percent.”

(B) The reference to “20 percent” in Section 41(a)(2) of the Internal Revenue Code is modified to read “24 percent.”

(3) For each taxable year beginning on or after January 1, 2000, both of the following shall apply:

(A) The reference to “20 percent” in Section 41(a)(1) of the Internal Revenue Code is modified to read “15 percent.”

(B) The reference to “20 percent” in Section 41(a)(2) of the Internal Revenue Code is modified to read “24 percent.”

(c) (1) With respect to any expense paid or incurred after the operative date of Section 6378, Section 41(b)(1) of the Internal Revenue Code is modified to exclude from the definition of “qualified research expense” any amount paid or incurred for tangible personal property that is eligible for the exemption from sales or use tax provided by Section 6378.

(2) “Qualified research” and “basic research” shall include only research conducted in California.

(d) The provisions of Section 41(e)(7)(A) of the Internal Revenue Code, shall be modified so that “basic research,” for purposes of this section, includes any basic or applied research including scientific inquiry or original investigation for the advancement of scientific or engineering knowledge or the

1 improved effectiveness of commercial products, except that the  
2 term does not include any of the following:

3 (1) Basic research conducted outside California.

4 (2) Basic research in the social sciences, arts, or humanities.

5 (3) Basic research for the purpose of improving a commercial  
6 product if the improvements relate to style, taste, cosmetic, or  
7 seasonal design factors.

8 (4) Any expenditure paid or incurred for the purpose of  
9 ascertaining the existence, location, extent, or quality of any  
10 deposit of ore or other mineral (including oil and gas).

11 (e) (1) In the case of a taxpayer engaged in any  
12 biopharmaceutical research activities that are described in codes  
13 2833 to 2836, inclusive, or any research activities that are  
14 described in codes 3826, 3829, or 3841 to 3845, inclusive, of the  
15 Standard Industrial Classification (SIC) Manual published by the  
16 United States Office of Management and Budget, 1987 edition, or  
17 any other biotechnology research and development activities, the  
18 provisions of Section 41(e)(6) of the Internal Revenue Code shall  
19 be modified to include both of the following:

20 (A) A qualified organization as described in Section  
21 170(b)(1)(A)(iii) of the Internal Revenue Code and owned by an  
22 institution of higher education as described in Section 3304(f) of  
23 the Internal Revenue Code.

24 (B) A charitable research hospital owned by an organization  
25 that is described in Section 501(c)(3) of the Internal Revenue  
26 Code, is exempt from taxation under Section 501(a) of the Internal  
27 Revenue Code, is not a private foundation, is designated a  
28 “specialized laboratory cancer center,” and has received Clinical  
29 Cancer Research Center status from the National Cancer Institute.

30 (2) For purposes of this subdivision:

31 (A) “Biopharmaceutical research activities” means those  
32 activities that use organisms or materials derived from organisms,  
33 and their cellular, subcellular, or molecular components, in order  
34 to provide pharmaceutical products for human or animal  
35 therapeutics and diagnostics. Biopharmaceutical activities make  
36 use of living organisms to make commercial products, as opposed  
37 to pharmaceutical activities that make use of chemical compounds  
38 to produce commercial products.

39 (B) “Other biotechnology research and development  
40 activities” means research and development activities consisting



1 of the application of recombinant DNA technology to produce  
2 commercial products, as well as research and development  
3 activities regarding pharmaceutical delivery systems designed to  
4 provide a measure of control over the rate, duration, and site of  
5 pharmaceutical delivery.

6 (f) In the case where the credit allowed by this section exceeds  
7 the “tax,” the excess may be carried over to reduce the “tax” in  
8 the following year, and succeeding years if necessary, until the  
9 credit has been exhausted.

10 (g) For each taxable year beginning on or after January 1, 1998,  
11 the reference to “Section 501(a)” in Section 41(b)(3)(C) of the  
12 Internal Revenue Code, relating to contract research expenses, is  
13 modified to read “this part or Part 10 (commencing with Section  
14 17001).”

15 (h) (1) ~~For each taxable year beginning on or after January 1,~~  
16 ~~1998, and before January 1, 2000:~~

17 (A) ~~The reference to “1.65 percent” in Section 41(c)(4)(A)(i)~~  
18 ~~of the Internal Revenue Code is modified to read “one and~~  
19 ~~thirty-two hundredths of one percent.”~~

20 (B) ~~The reference to “2.2 percent” in Section 41(c)(4)(A)(ii)~~  
21 ~~of the Internal Revenue Code is modified to read “one and~~  
22 ~~seventy-six hundredths of one percent.”~~

23 (C) ~~The reference to “2.75 percent” in Section 41(c)(4)(A)(iii)~~  
24 ~~of the Internal Revenue Code is modified to read “two and~~  
25 ~~two-tenths of one percent.”~~

26 (2) ~~For each taxable year beginning on or after January 1, 2000:~~

27 (A) The reference to ~~“1.65~~ “2.65 percent” in Section  
28 41(c)(4)(A)(i) of the Internal Revenue Code is modified to read  
29 “one and forty-nine hundredths of one percent.”

30 (B) The reference to ~~“2.2~~ “3.2 percent” in Section  
31 41(c)(4)(A)(ii) of the Internal Revenue Code is modified to read  
32 “one and ninety-eight hundredths of one percent.”

33 (C) The reference to ~~“2.75~~ “3.75 percent” in Section  
34 41(c)(4)(A)(iii) of the Internal Revenue Code is modified to read  
35 “two and forty-eight hundredths of one percent.”

36 (3) ~~—~~

37 (2) Section 41(c)(4)(B) shall not apply and in lieu thereof an  
38 election under Section 41(c)(4)(A) of the Internal Revenue Code  
39 may be made for any taxable year of the taxpayer beginning on or  
40 after January 1, 1998. That election shall apply to the taxable year

1 for which made and all succeeding taxable years unless revoked  
2 with the consent of the Franchise Tax Board.

3 ~~(4)–~~

4 (3) Section 41(c)(6) of the Internal Revenue Code, relating to  
5 gross receipts, is modified to take into account only those gross  
6 receipts from the sale of property held primarily for sale to  
7 customers in the ordinary course of the taxpayer's trade or business  
8 that is delivered or shipped to a purchaser within this state,  
9 regardless of f.o.b. point or any other condition of the sale.

10 (i) Section 41(h) of the Internal Revenue Code, relating to  
11 termination, shall not apply.

12 (j) Section 41(g) of the Internal Revenue Code, relating to  
13 special rule for passthrough of credit, is modified by each of the  
14 following:

15 (1) The last sentence shall not apply.

16 (2) If the amount determined under Section 41(a) of the  
17 Internal Revenue Code for any taxable year exceeds the limitation  
18 of Section 41(g) of the Internal Revenue Code, that amount may  
19 be carried over to other taxable years under the rules of subdivision  
20 (f), except that the limitation of Section 41(g) of the Internal  
21 Revenue Code shall be taken into account in each subsequent  
22 taxable year.

23 *SEC. 37.* Section 23701s of the Revenue and Taxation Code  
24 is amended to read:

25 23701s. (a) An employee-funded pension trust described in  
26 Section 501(c)(18) of the Internal Revenue Code, except as  
27 otherwise provided.

28 (b) The last sentence in Section 501(c)(18) of the Internal  
29 Revenue Code, as amended by Title VI of the Economic Growth  
30 and Tax Relief Reconciliation Act of 2001 (Public Law 107-16),  
31 relating to excess contributions under Section 4979, shall not  
32 apply.

33 ~~SEC. 30.—~~

34 *SEC. 38.* Section 23705 of the Revenue and Taxation Code is  
35 amended to read:

36 23705. (a) (1) An organization described in Section 23701i  
37 (voluntary employee's beneficiary associations) or 23701q  
38 (qualified group legal service plans) which is part of a plan of an  
39 employer shall not be exempt from tax under Section 23701,  
40 unless that plan meets the requirements of Section 505(b) of the

Internal Revenue Code, as amended by Title VI of the Economic Growth and Tax Relief Reconciliation Act of 2001 (Public Law 107-16).

(2) Paragraph (1) shall not apply to any organization described in Section 505(a)(2) of the Internal Revenue Code.

(b) A copy of any notice filed with the Secretary of the Treasury, pursuant to Section 505(c) of the Internal Revenue Code, relating to application for tax-exempt status, shall be filed at the same time and in the same manner with the Franchise Tax Board.

~~SEC. 31.~~

*SEC. 39.* Section 23711 of the Revenue and Taxation Code is amended to read:

23711. Section 529 of the Internal Revenue Code, as amended by Section 402 of the Economic Growth and Tax Relief Reconciliation Act of 2001 (Public Law 107-16) relating to qualified state tuition programs, shall apply, except as otherwise provided.

(a) Section 529(a) of the Internal Revenue Code is modified as follows:

(1) By substituting the phrase “under Part 10 (commencing with Section 17001) and this part” in lieu of the phrase “under this subtitle.”

(2) By substituting “Article 2 (commencing with Section 23731)” in lieu of “section 511.”

(b) A copy of the report required to be filed with the Secretary of the Treasury under Section 529(d) of the Internal Revenue Code shall be filed with the Franchise Tax Board at the same time and in the same manner as specified in that section.

~~SEC. 32.~~

*SEC. 40.* Section 23712 of the Revenue and Taxation Code is amended to read:

23712. Section 530 of the Internal Revenue Code, as amended by Sections 401 and 402 of the Economic Growth and Tax Relief Reconciliation Act of 2001 (Public Law 107-16) relating to education individual retirement accounts, shall apply, except as otherwise provided.

(a) Section 530(a) of the Internal Revenue Code is modified as follows:

1 (1) By substituting the phrase “under Part 10 (commencing  
2 with Section 17001) and this part” in lieu of the phrase “under this  
3 subtitle.”

4 (2) By substituting “Article 2 (commencing with Section  
5 23731)” in lieu of “section 511.”

6 (b) For taxable years beginning before January 1, 2002,  
7 Section 530(b)(1) of the Internal Revenue Code, relating to the  
8 definition of education individual retirement account, is modified  
9 to additionally require that upon the date that the designated  
10 beneficiary becomes 30 years of age, any balance to the credit of  
11 the beneficiary shall be distributed within 30 days after the date the  
12 beneficiary becomes 30 years of age to that beneficiary.

13 (c) Section 530(d) of the Internal Revenue Code is modified as  
14 follows:

15 (1) By substituting the phrase “under Part 10 (commencing  
16 with Section 17001) in the manner as provided in Section 72(b) of  
17 the Internal Revenue Code, as modified by Part 10” in lieu of the  
18 phrase “in the manner as provided in Section 72(b)” in Section  
19 530(d)(1) of the Internal Revenue Code.

20 (2) (A) A taxpayer that has elected to waive the application of  
21 Section 530(d)(2) of the Internal Revenue Code for federal income  
22 tax purposes shall be treated as having waived the application of  
23 that paragraph for state purposes, a separate election for state  
24 purposes shall not be allowed under paragraph (3) of subdivision  
25 (e) of Section 17024.5 or paragraph (3) of subdivision (e) of  
26 Section 23051.5, and the federal election shall be binding for  
27 purposes of Part 10 (commencing with Section 17001) and this  
28 part.

29 (B) If a taxpayer fails to make an election under Section  
30 530(d)(2)(C) of the Internal Revenue Code for federal income tax  
31 purposes to waive the application of Section 530(d)(2) of the  
32 Internal Revenue Code, an election under Section 530(d)(2)(C) of  
33 the Internal Revenue Code shall not be allowed for state purposes,  
34 Section 530(d)(2)(A) and (B) of the Internal Revenue Code shall  
35 apply for state purposes, and a separate election for state purposes  
36 shall not be allowed under paragraph (3) of subdivision (e) of  
37 Section 17024.5.

38 (3) (A) By substituting the phrase “tax imposed by Part 10  
39 (commencing with Section 17001)” in lieu of the phrase “tax

imposed by this chapter” in Section 530(d)(4)(A) of the Internal Revenue Code.

(B) By substituting the phrase “increased by 2<sup>1</sup>/<sub>2</sub> percent” in lieu of the phrase “increased by 10 percent” in Section 530(d)(4)(A) of the Internal Revenue Code.

(C) By substituting the phrase “shall be included in the contributor’s gross income under Part 10 (commencing with Section 17001) or this part” in lieu of the phrase “shall be included in gross income” in Section 530(d)(4)(C) of the Internal Revenue Code.

(d) For purposes of Part 10 (commencing with Section 17001) and this part, in the case of a custodial account treated as a trust by reason of Section 530(g) of the Internal Revenue Code, the custodian of that account shall be treated as the trustee thereof.

(e) A copy of the report, which is required to be filed with the Secretary of the Treasury under Section 530(h) of the Internal Revenue Code, shall be filed with the Franchise Tax Board at the same time and in the same manner as specified in that section.

~~SEC. 33.—Section 23800.5 of the Revenue and Taxation Code is amended to read:~~

~~23800.5.—(a) Section 1361(b)(2)(A) of the Internal Revenue Code, relating to ineligible corporation defined, shall not apply and in lieu thereof, for purposes of Section 1361(b)(1) of the Internal Revenue Code, Part 10 (commencing with Section 17001), Part 10.2 (commencing with Section 18401), and this part, “ineligible corporation” shall include a savings and loan association, bank, or financial corporation which uses the reserve method of accounting for bad debts described in Section 24348.~~

~~(b) Section 1361(b)(3) of the Internal Revenue Code, relating to treatment of certain wholly owned subsidiaries, is modified as follows:~~

~~(1) For purposes of Part 10 (commencing with Section 17001), Part 10.2 (commencing with Section 18401), and this part:~~

~~(A) Section 1361(b)(3)(A)(i) of the Internal Revenue Code shall apply, except as provided in subparagraph (B).~~

~~(B) There is hereby imposed a tax annually in an amount equal to the applicable amount specified in paragraph (1) of subdivision (d) of Section 23153 on a qualified Subchapter S subsidiary that is incorporated under the laws of this state, qualified to transact intrastate business in this state pursuant to Chapter 21~~

~~(commencing with Section 2100) of Division 1 of Title 1 of the Corporations Code, or doing business in this state.~~

~~(C) Every qualified Subchapter S subsidiary described in subparagraph (B) shall be subject to the tax imposed under subparagraph (B) from the earlier of the date of incorporation, qualification, or commencement of business in this state, until the effective date of dissolution or withdrawal as provided in Section 23331, or, if later, the date the corporation ceases to do business in this state.~~

~~(2) For purposes of Part 10 (commencing with Section 17001), Part 10.2 (commencing with Section 18401), and this part:~~

~~(A) Section 1361(b)(3)(A)(ii) of the Internal Revenue Code shall not apply and, in lieu thereof, subparagraph (B) shall apply and all references to Section 1361(b)(3)(A)(ii) of the Internal Revenue Code shall be treated as a reference to subparagraph (B):~~

~~(B) All activities, assets, liabilities, including liability for the tax imposed under this subdivision, and items of income, deduction, and credit of a qualified Subchapter S subsidiary shall be treated as activities (including activities for purposes of Section 23101), assets, liabilities, and those items, as the case may be, of the "S corporation."~~

~~(3) Section 1361(b)(3)(B) of the Internal Revenue Code is modified to include the following requirements in addition to the requirements contained therein:~~

~~(A) The "S corporation" has in effect a valid election to treat the corporation as a qualified Subchapter S subsidiary for federal income tax purposes:~~

~~(B) An election made by the "S corporation" under Section 1361(b)(3)(B)(ii) of the Internal Revenue Code to treat the corporation as a qualified Subchapter S subsidiary for federal income tax purposes shall be treated for purposes of this part as an election made by the "S corporation" under this subdivision and a separate election shall not be allowed.~~

~~(C) No election under this subdivision shall be allowed unless the "S corporation" has made the election under Section 1361(b)(3)(B)(ii) of the Internal Revenue Code to treat the corporation as a qualified Subchapter S subsidiary for federal income tax purposes.~~

~~(c) Section 1361(e)(6) of the Internal Revenue Code, relating to certain exempt organizations permitted as shareholders, is~~

~~modified by substituting a reference to Section 17631 or Section 23701d in lieu of the reference to Section 501(e)(3) of the Internal Revenue Code and by substituting a reference to Section 17631 or Section 23701 in lieu of the reference to Section 501(a) of the Internal Revenue Code.~~

~~(d) Section 1361(e)(1)(B)(ii) of the Internal Revenue Code, relating to certain trusts not eligible, is modified by substituting “under Part 10 (commencing with Section 17001) or this part” in lieu of “under this subtitle.”~~

~~(e) Section 1361(e)(3) of the Internal Revenue Code, relating to election, is modified to include the following provisions:~~

~~(1) An election made by the trustee under Section 1361(e) of the Internal Revenue Code to be an electing small business trust for federal income tax purposes shall be treated for purposes of this part as an election made by the trustee under this subdivision and a separate election shall not be allowed. Any election made shall apply to the taxable year of the trust for which made and to all subsequent taxable years of the trust, unless revoked with the consent of the Franchise Tax Board.~~

~~(2) No election under this subdivision shall be allowed unless the trustee has made the election under Section 1361(e) of the Internal Revenue Code to be an electing small business trust for federal income tax purposes.~~

~~SEC. 34.—~~

~~SEC. 41. Section 23801 of the Revenue and Taxation Code is amended to read:~~

~~23801. (a) Except as otherwise provided, a corporation that has in effect for federal income tax purposes a valid election under Section 1362(a) of the Internal Revenue Code shall be an “S corporation” for purposes of Part 10 (commencing with Section 17001), Part 10.2 (commencing with Section 18401), and this part.~~

~~(b) A corporation that is an “S corporation” for federal income tax purposes, shall be an “S corporation” for purposes of Part 10 (commencing with Section 17001), Part 10.2 (commencing with Section 18401, and this part, and its shareholders shall be *shareholders* of an “S corporation” without regard to whether the corporation is qualified to do business or is incorporated in this state.~~

~~(c) Notwithstanding subdivision (a), a corporation that elects “S corporation” status under Section 1362 of the Internal Revenue~~



1 Code for federal income tax purposes but which is not qualified to  
2 be an “S corporation” under subdivision (a) of Section 23800.5,  
3 shall not be an “S corporation” for purposes of Part 10  
4 (commencing with Section 17001), Part 10.2 (commencing with  
5 Section 18401, and this part.

6 (d) Except as provided in subdivision (e), a corporation *that* is  
7 an “S corporation” for purposes of this part shall not be included  
8 in a combined report pursuant to Chapter 17 (commencing with  
9 Section 25101).

10 (e) (1) In cases where the Franchise Tax Board determines that  
11 the reported income or loss of a group of commonly owned or  
12 controlled corporations (within the meaning of Section 25105),  
13 which includes one or more corporations treated as an “S  
14 corporation” under Chapter 4.5 (commencing with Section  
15 23800), does not clearly reflect income (or loss) of a member of  
16 that group or represents an evasion of tax by one or more members  
17 of that group, and the Franchise Tax Board determines that the  
18 comparable uncontrolled price method prescribed by regulations  
19 pursuant to Section 482 of the Internal Revenue Code cannot  
20 practically be applied, the Franchise Tax Board may, in lieu of  
21 other methods prescribed by regulations pursuant to Section 482  
22 of the Internal Revenue Code, apply methods of unitary  
23 combination, pursuant to Article 1 (commencing with Section  
24 25101) of Chapter 17, to properly reflect the income or loss of the  
25 members of the group.

26 (2) The application of the provisions of this subdivision shall  
27 not affect the treatment of any corporation as an “S corporation.”

28 (f) The tax for a “C corporation” for a short year shall be  
29 determined in accordance with Chapter 13 (commencing with  
30 Section 24631), in lieu of Section 1362(e)(5) of the Internal  
31 Revenue Code.

32 (g) (1) A termination of a federal election pursuant to Section  
33 1362(d) of the Internal Revenue Code, that is not an inadvertent  
34 termination pursuant to Section 1362(f) of the Internal Revenue  
35 Code, shall simultaneously terminate the “S corporation” election  
36 for purposes of Part 10 (commencing with Section 17001), Part  
37 10.2 (commencing with Section 18401), and this part.

38 (2) A federal termination by revocation shall be effective for  
39 purposes of this part and shall be reported to the Franchise Tax  
40 Board in the form and manner prescribed by the Franchise Tax

1 Board no later than the last date allowed for filing federal  
2 termination for that year under Section 1362(d) of the Internal  
3 Revenue Code.

4 (h) For taxable years beginning on or after January 1, 1997, for  
5 purposes of subparagraph (F) of paragraph (4) of subdivision (a)  
6 of this section and Section 1362(g) of the Internal Revenue Code,  
7 relating to election after termination, any termination under  
8 Section 1362(d) of the Internal Revenue Code or election to be  
9 treated as a “C corporation” under subparagraph (A) or (C) of  
10 paragraph (4) of subdivision (a), or to terminate by revocation  
11 under paragraph (3) of subdivision (f) in a taxable year beginning  
12 before January 1, 1997, shall not be taken into account.

13 (i) (1) The provisions of Section 1362(b)(5) of the Internal  
14 Revenue Code, relating to authority to treat late elections, etc., as  
15 timely, shall apply only for taxable years beginning on or after  
16 January 1, 1997, with respect to elections under Section 1362(a)  
17 of the Internal Revenue Code for taxable years beginning on or  
18 after January 1, 1997.

19 (2) Notwithstanding the provisions of paragraph (1), if for any  
20 taxable year beginning on or after January 1, 1987, a corporation  
21 fails to qualify as an “S corporation” for federal income tax  
22 purposes solely because the federal Form 2553 (Election by a  
23 Small Business Corporation) was not filed timely, the corporation  
24 shall be treated for purposes of this part as an “S corporation” for  
25 the taxable year the “S corporation” election should have been  
26 made, and for each subsequent year until terminated, if both of the  
27 following conditions are met:

28 (A) The corporation and all of its shareholders reported their  
29 income for California tax purposes on original returns consistent  
30 with “S corporation” status for the year the “S corporation”  
31 election should have been made, and for each subsequent taxable  
32 year (if any) until terminated.

33 (B) The corporation and its shareholders have filed with the  
34 Internal Revenue Service a federal Form 2553 requesting  
35 automatic relief with respect to the late “S corporation” election,  
36 in full compliance with the federal Revenue Procedure 1997-48,  
37 I.R.B. 1997-43, and have received notification of the acceptance  
38 of the untimely filed “S corporation” election from the Internal  
39 Revenue Service. A copy of the notification shall be provided to  
40 the Franchise Tax Board upon request.

(j) The provisions of Section 1362(f) of the Internal Revenue Code, relating to inadvertent invalid elections or terminations, shall apply only for taxable years beginning on or after January 1, 1997, with respect to elections under Section 1362(a) of the Internal Revenue Code for taxable years beginning on or after January 1, 1997.

~~SEC. 35.—~~

SEC. 42. Section 23802 of the Revenue and Taxation Code is amended to read:

23802. (a) Section 1363(a) of the Internal Revenue Code, relating to the taxability of an “S corporation,” shall not be applicable.

(b) Corporations qualifying under this chapter shall continue to be subject to the taxes imposed under Chapter 2 (commencing with Section 23101) and Chapter 3 (commencing with Section 23501), except as follows:

(1) The tax imposed under Section 23151 or 23501 shall be imposed at a rate of  $1\frac{1}{2}$  percent rather than the rate specified in those sections.

(2) In the case of an “S corporation” which is also a financial corporation, the rate of tax specified in paragraph (1) shall be increased by the excess of the rate imposed under Section 23183 over the rate imposed under Section 23151.

(c) An “S corporation” shall be subject to the minimum franchise tax imposed under Section 23153.

(d) (1) For purposes of subdivision (b), an “S corporation” shall be allowed a deduction under Section 24416 or 24416.1 (relating to net operating loss deductions), but only with respect to losses incurred during periods in which the corporation is an “S corporation” for purposes of this part.

(2) Section 1371(b) of the Internal Revenue Code, relating to denial of carryovers between “C years” and “S years,” shall apply for purposes of the tax imposed under subdivision (b), except as provided in paragraph (1).

(3) The provisions of this subdivision shall not affect the amount of any item of income or loss computed in accordance with the provisions of Section 1366 of the Internal Revenue Code, relating to passthrough items to shareholders.

(4) For purposes of subdivision (b) of Section 17276, relating to limitations on loss carryovers, losses passed through to

1 shareholders of an “S corporation,” to the extent otherwise  
2 allowable without application of that subdivision, shall be fully  
3 included in the net operating loss of that shareholder and then that  
4 subdivision shall be applied to the entire net operating loss.

5 (e) For purposes of computing the taxes specified in  
6 subdivision (b), an “S corporation” shall be allowed a deduction  
7 from income for built-in gains and passive investment income for  
8 which a tax has been imposed under this part in accordance with  
9 the provisions of Section 1374 of the Internal Revenue Code,  
10 relating to tax imposed on certain built-in gains, or Section 1375  
11 of the Internal Revenue Code, relating to tax imposed on passive  
12 investment income.

13 (f) For purposes of computing taxes imposed under this part, as  
14 provided in subdivision (b):

15 (1) An “S corporation” shall compute its deductions for  
16 amortization and depreciation in accordance with the provisions  
17 of Part 10 (commencing with Section 17001) of Division 2.

18 (2) The provisions of Section 465 of the Internal Revenue  
19 Code, relating to limitation of deductions to the amount at risk,  
20 shall be applied in the same manner as in the case of an individual.

21 (3) (A) The provisions of Section 469 of the Internal Revenue  
22 Code, relating to limitations on passive activity losses and credits,  
23 shall be applied in the same manner as in the case of an individual.  
24 For purposes of the tax imposed under Section 23151 or 23501, as  
25 modified by this section, material participation shall be  
26 determined in accordance with Section 469(h) of the Internal  
27 Revenue Code, relating to certain closely held “C corporations”  
28 and personal service corporations.

29 (B) For purposes of this paragraph, the “adjusted gross  
30 income” of the “S corporation” shall be equal to its “net  
31 income,” as determined under Section 24341 with the  
32 modifications required by this subdivision, except that no  
33 deduction shall be allowed for contributions allowed by Section  
34 24357.

35 (4) The exclusion provided under Section 18152.5 shall not be  
36 allowed to an “S corporation.”

37 (g) The provisions of Section 1363(d) of the Internal Revenue  
38 Code, relating to recapture of LIFO benefits, shall be modified for  
39 purposes of this part to refer to Section 19101 in lieu of Section  
40 6601 of the Internal Revenue Code.

1 ~~SEC. 36.— Section 23806 of the Revenue and Taxation Code is~~  
2 ~~amended to read:~~

3 ~~23806.— (a) Section 1371(a) of the Internal Revenue Code,~~  
4 ~~relating to application of Subchapter C rules, is modified to~~  
5 ~~provide that any election by an “S corporation” or its shareholders~~  
6 ~~under Section 338 of the Internal Revenue Code, relating to certain~~  
7 ~~stock purchases treated as asset acquisitions, for federal income~~  
8 ~~tax purposes shall be treated as an election for purposes of Part 10~~  
9 ~~(commencing with Section 17001, Part 10.2 (commencing with~~  
10 ~~Section 18401), and this part and a separate election for state~~  
11 ~~purposes shall not be allowed.~~

12 ~~(b) No election under Section 338 of the Internal Revenue~~  
13 ~~Code, relating to certain stock purchases treated as asset~~  
14 ~~acquisitions, shall be allowed for state purposes unless the “S~~  
15 ~~corporation” or its shareholders made a valid election for federal~~  
16 ~~income tax purposes under Section 338 of the Internal Revenue~~  
17 ~~Code.~~

18 ~~(c) Section 1371 (d) of the Internal Revenue Code shall not~~  
19 ~~apply.~~

20 ~~SEC. 37.—~~

21 *SEC. 43.* Section 23811 of the Revenue and Taxation Code is  
22 amended to read:

23 23811. Except as otherwise provided in this section, there is  
24 hereby imposed a tax on passive investment income attributable to  
25 California sources, determined in accordance with the provisions  
26 of Section 1375 of the Internal Revenue Code, relating to tax  
27 imposed on passive investment income, as modified by this  
28 section.

29 (a) The tax imposed under this section shall not be imposed on  
30 an “S corporation” that has no excess net passive income for  
31 federal income tax purposes determined in accordance with  
32 Section 1375 of the Internal Revenue Code.

33 (b) (1) The rate of tax shall be equal to the rate of tax imposed  
34 under Section 23151 in lieu of Section 11(b) of the Internal  
35 Revenue Code.

36 (2) In the case of an “S corporation” which is also a financial  
37 corporation, the rate of tax specified in paragraph (1) shall be  
38 increased by the excess of the rate imposed under Section 23183  
39 over the rate imposed under Section 23151.

(c) The provisions of Section 1375(c)(1) of the Internal Revenue Code, relating to credits, shall be modified to provide that the tax imposed under subdivision (a) shall not be reduced by any credits allowed under this part.

(d) The term “subchapter C earnings and profits” as used in Sections 1362(d)(3) and 1375 of the Internal Revenue Code shall mean the subchapter C earnings and profits of the corporation attributable to California sources determined under this part, modified as provided in subdivision (e).

(e) (1) In the case of a corporation which is an “S corporation” for purposes of this part for its first taxable year for which it has in effect a valid federal S election, there shall be allowed as a deduction in determining that corporation’s subchapter C earnings and profits at the close of any taxable year the amount of any consent dividend (as provided in paragraph (2)) paid after the close of that taxable year.

(2) In the event there is a determination that a corporation described in paragraph (1) has subchapter C earnings and profits at the close of any taxable year, that corporation shall be entitled to distribute a consent dividend to its shareholders. The amount of the consent dividend shall not exceed the difference between the corporation’s subchapter C earnings and profits determined under subdivision (d) at the close of the taxable year with respect to which the determination is made and the corporation’s subchapter C earnings and profits for federal income tax purposes at the same date. A consent dividend must be paid within 90 days of the date of the determination that the corporation has subchapter C earnings and profits. For this purpose, the date of a determination means the effective date of a closing agreement pursuant to Section 19441, the date an assessment of tax imposed by this section becomes final, or the date of execution by the corporation of an agreement with the Franchise Tax Board relating to liability for the tax imposed by this section. For purposes of Part 10 (commencing with Section 17001), Part 10.2 (commencing with Section 18401), and this part, a corporation must make the election provided in Section 1368(e)(3) of the Internal Revenue Code for federal income tax purposes any consent dividend.

(3) If a corporation distributes a consent dividend, it shall claim the deduction provided in paragraph (1) by filing a claim therefor

1 with the Franchise Tax Board within 120 days of the date of the  
2 determination specified in paragraph (2).

3 (4) The collection of tax imposed by this section from a  
4 corporation described in paragraph (2) shall be stayed for 120 days  
5 after the date of the determination specified in paragraph (2). If a  
6 claim is filed pursuant to paragraph (3), collection of that tax shall  
7 be further stayed until the date the claim is acted upon by the  
8 Franchise Tax Board.

9 (5) If a claim is filed pursuant to paragraph (3), the running of  
10 the statute of limitations on the making of assessments and actions  
11 for collection of the tax imposed by this section shall be suspended  
12 for a period of two years after the date of the determination  
13 specified in paragraph (2).

14 ~~SEC. 37.5. Section 24273 of the Revenue and Taxation Code~~  
15 ~~is amended to read:~~

16 ~~24273. Amounts received as loans from the Commodity~~  
17 ~~Credit Corporation shall be considered as income and shall be~~  
18 ~~included in gross income for the taxable year in which received,~~  
19 ~~if the taxpayer has made an election pursuant to Section 77 of the~~  
20 ~~Internal Revenue Code for federal income tax purposes with~~  
21 ~~respect to loans received from the Commodity Credit Corporation.~~

22 ~~SEC. 38. Section 24307 of the Revenue and Taxation Code is~~  
23 ~~amended to read:~~

24 ~~24307. (a) Section 108 of the Internal Revenue Code,~~  
25 ~~relating to income from discharge of indebtedness, shall apply,~~  
26 ~~except as otherwise provided.~~

27 ~~(b) Section 108(b)(2)(B) of the Internal Revenue Code,~~  
28 ~~relating to general business credit, is modified by substituting~~  
29 ~~“this part” in lieu of “Section 38 (relating to general business~~  
30 ~~credit).”~~

31 ~~(c) Section 108(b)(2)(G) of the Internal Revenue Code,~~  
32 ~~relating to foreign tax credit carryovers, shall not apply.~~

33 ~~(d) Section 108(b)(3)(B) of the Internal Revenue Code,~~  
34 ~~relating to credit carryover reduction, is modified by substituting~~  
35 ~~“11.1 cents” in lieu of “33 1/3 cents” in each place in which it~~  
36 ~~appears. In the case where more than one credit is allowable under~~  
37 ~~this part, the credits shall be reduced on a pro rata basis.~~

38 ~~(e) Section 108(g)(3)(B) of the Internal Revenue Code,~~  
39 ~~relating to adjusted tax attributes, is modified by substituting “\$9”~~  
40 ~~in lieu of “\$3.”~~



~~(f) (1) The amendments to Section 108 of the Internal Revenue Code made by Section 13150 of the Revenue Reconciliation Act of 1993 (Public Law 103-66), relating to exclusion from gross income for income from discharge of qualified real property business indebtedness, shall apply to discharges occurring on or after January 1, 1996, in taxable years beginning on or after January 1, 1996.~~

~~(2) If a taxpayer makes an election for federal income tax purposes under Section 108(c) of the Internal Revenue Code, relating to treatment of discharge of qualified real property business indebtedness, a separate election shall not be allowed and the federal election shall be binding for purposes of this part.~~

~~(3) If a taxpayer has not made an election for federal income tax purposes under Section 108(c) of the Internal Revenue Code, relating to treatment of discharge of qualified real property business indebtedness, then the taxpayer shall not be allowed to make that election for purposes of this part.~~

~~(g) The amendments to Section 108 of the Internal Revenue Code made by Section 13226 of the Revenue Reconciliation Act of 1993 (Public Law 103-66), relating to modifications of discharge of indebtedness provisions, shall apply to discharges occurring on or after January 1, 1996, in taxable years beginning on or after January 1, 1996.~~

~~SEC. 39. Section 24347.6 is added to the Revenue and Taxation Code, to read:~~

~~24347.6. Notwithstanding subdivision (e) of Section 23051.5, a taxpayer may make a separate state election under Section 165(i)(1) of the Internal Revenue Code to take a loss attributable to a disaster into account in the taxable year immediately preceding the taxable year in which the disaster occurred.~~

~~SEC. 40. Section 24349 of the Revenue and Taxation Code is amended to read:~~

~~24349. (a) There shall be allowed as a depreciation deduction a reasonable allowance for the exhaustion, wear, and tear (including a reasonable allowance for obsolescence)—~~

~~(1) Of property used in the trade or business; or~~

~~(2) Of property held for the production of income.~~

~~(b) Except as otherwise provided in subdivision (c), for taxable years ending after December 31, 1958, the term “reasonable~~

allowance” as used in subdivision (a) shall include, but shall not be limited to, an allowance computed in accordance with regulations prescribed by the Franchise Tax Board, under any of the following methods:

(1) The straight-line method.

(2) The declining balance method, using a rate not exceeding twice the rate that would have been used had the annual allowance been computed under the method described in paragraph (1).

(3) The sum of the years digits method.

(4) Any other consistent method productive of an annual allowance that, when added to all allowances for the period commencing with the taxpayer’s use of the property and including the taxable year, does not, during the first two-thirds of the useful life of the property, exceed the total of those allowances that would have been used had those allowances been computed under the method described in paragraph (2).

Nothing in this subdivision shall be construed to limit or reduce an allowance otherwise allowable under subdivision (a).

(c) Any grapevine replaced in a vineyard in California in a taxable year beginning on or after January 1, 1992, as a direct result of a phylloxera infestation in that vineyard, and any grapevine replaced in a vineyard in California in a taxable year beginning on or after January 1, 1997, as a direct result of Pierce’s disease in that vineyard, shall have a useful life of five years, except that it shall have a class life of 10 years for purposes of depreciation under Section 168(g)(2) of the Internal Revenue Code where the taxpayer has made an election under Section 263A(d)(3) of the Internal Revenue Code not to capitalize costs of the infested vineyard. Every taxpayer claiming a deduction under this section with respect to a grapevine as described in this subdivision shall obtain a written certification from an independent state-certified integrated pest management adviser, or a state agricultural commissioner or adviser, that specifies that the replanting was necessary to restore a vineyard infested with phylloxera or Pierce’s disease. The taxpayer shall retain the certification for future audit purposes.

(d) For purposes of this part, the deduction for property leased to governments and other tax-exempt entities, as defined in Section 168(h) of the Internal Revenue Code, shall be limited to the amount determined under Section 168(g) of the Internal

1 ~~Revenue Code, relating to alternative depreciation system for~~  
2 ~~certain property.~~

3 ~~(e) (1) In the case of any building erected or improvements~~  
4 ~~made on leased property, if the building or improvement is~~  
5 ~~property to which this section applies, the depreciation deduction~~  
6 ~~shall be determined under the provisions of this section.~~

7 ~~(2) An improvement shall be treated for purposes of~~  
8 ~~determining gain or loss under this part as disposed of by the lessor~~  
9 ~~when so disposed of or abandoned if both of the following occur:~~

10 ~~(A) The improvement is made by the lessor of leased property~~  
11 ~~for the lessee of that property.~~

12 ~~(B) The improvement is irrevocably disposed of or abandoned~~  
13 ~~by the lessor at the termination of the lease by the lessee.~~

14 ~~This subdivision shall not apply to any property to which~~  
15 ~~Section 168 of the Internal Revenue Code does not apply for~~  
16 ~~federal income tax purposes by reason of Section 168(f) of the~~  
17 ~~Internal Revenue Code. Any election made under Section~~  
18 ~~168(f)(1) of the Internal Revenue Code for federal income tax~~  
19 ~~purposes with respect to that property shall be treated as a binding~~  
20 ~~election for state purposes under this subdivision with respect to~~  
21 ~~that same property and no separate election with respect to that~~  
22 ~~property shall be allowed.~~

23 ~~(3) (A) In determining a lease term, both of the following shall~~  
24 ~~apply:~~

25 ~~(i) There shall be taken into account options to renew.~~

26 ~~(ii) Two or more successive leases which are part of the same~~  
27 ~~transaction (or a series of related transactions) with respect to the~~  
28 ~~same or substantially similar property shall be treated as one lease.~~

29 ~~(B) For purposes of clause (i) of subparagraph (A), in the case~~  
30 ~~of nonresidential real property or residential rental property, there~~  
31 ~~shall not be taken into account any option to renew at fair market~~  
32 ~~value determined at the time of renewal.~~

33 ~~(f) (1) Section 167(g) of the Internal Revenue Code, relating~~  
34 ~~to depreciation under income forecast method, shall apply except~~  
35 ~~as otherwise provided.~~

36 ~~(2) Section 167(g)(2)(C) of the Internal Revenue Code is~~  
37 ~~modified by substituting “Section 19521” in lieu of “Section~~  
38 ~~460(b)(7)” of the Internal Revenue Code.~~

39 ~~(3) Section 167(g)(5)(D) of the Internal Revenue Code is~~  
40 ~~modified by substituting “Part 10.2 (commencing with Section~~

1 ~~18401) (other than Article 2 (commencing with Section 19021)~~  
2 ~~and Sections 19142 to 19150, inclusive)” in lieu of “Subtitle F~~  
3 ~~(other than Sections 6654 and 6655).”~~

4 ~~SEC. 41. Section 24355.5 of the Revenue and Taxation Code~~  
5 ~~is amended to read:~~

6 ~~24355.5. (a) Section 197 of the Internal Revenue Code,~~  
7 ~~relating to amortization of goodwill and certain other intangibles,~~  
8 ~~shall apply, except as otherwise provided.~~

9 ~~(b) (1) Section 13261(g) of the Revenue Reconciliation Act of~~  
10 ~~1993 (Public Law 103-66), relating to effective dates, shall apply,~~  
11 ~~except as otherwise provided.~~

12 ~~(2) (A) If a taxpayer has, at any time, made an election for~~  
13 ~~federal income tax purposes under Section 13261(g)(2) of the~~  
14 ~~Revenue Reconciliation Act of 1993 (Public Law 103-66),~~  
15 ~~relating to election to have amendments apply to property acquired~~  
16 ~~after July 25, 1991, or Section 13261(g)(3) of that act, relating to~~  
17 ~~elective binding contract exception, a separate election for state~~  
18 ~~purposes shall not be allowed and the federal election shall be~~  
19 ~~binding for purposes of this part.~~

20 ~~(B) If a taxpayer has not made an election for federal income~~  
21 ~~tax purposes under Section 13261(g)(2) of the Revenue~~  
22 ~~Reconciliation Act of 1993 (Public Law 103-66), relating to~~  
23 ~~election to have amendments apply to property acquired after July~~  
24 ~~25, 1991, or Section 13261(g)(3) of that act, relating to elective~~  
25 ~~binding contract exception, with respect to property acquired~~  
26 ~~before August 11, 1993, then the taxpayer shall not be allowed to~~  
27 ~~make an election under Section 13261(g) of the Revenue~~  
28 ~~Reconciliation Act of 1993 (Public Law 103-66), for purposes of~~  
29 ~~this part, with respect to that property.~~

30 ~~(c) Notwithstanding any other provision of this section, each of~~  
31 ~~the following shall apply:~~

32 ~~(1) No deduction shall be allowed under this section for any~~  
33 ~~taxable year beginning prior to January 1, 1994.~~

34 ~~(2) No inference is intended with respect to the allowance or~~  
35 ~~denial of any deduction for amortization in any taxable year~~  
36 ~~beginning before January 1, 1994.~~

37 ~~(3) In the case of an intangible that was acquired in an taxable~~  
38 ~~year beginning before January 1, 1994, the amount to be amortized~~  
39 ~~shall not exceed the adjusted basis of that intangible as of the first~~  
40 ~~day of the first taxable year beginning on or after January 1, 1994,~~

1 ~~and that amount shall be amortized ratably over the period~~  
2 ~~beginning with the first month of the first taxable year beginning~~  
3 ~~on or after January 1, 1994, and ending 15 years after the month~~  
4 ~~in which the intangible was acquired.~~

5 SEC. 41.2. ~~Section 24357 of the Revenue and Taxation Code~~  
6 ~~is amended to read:~~

7 ~~24357. (a) There shall be allowed as a deduction any~~  
8 ~~charitable contribution (as defined in Section 24359) payment of~~  
9 ~~which is made within the taxable year. A charitable contribution~~  
10 ~~shall be allowable as a deduction only if verified under regulations~~  
11 ~~prescribed by the Franchise Tax Board.~~

12 ~~(b) In the case of a corporation reporting its income on the~~  
13 ~~accrual basis, the corporation shall treat the contribution as paid~~  
14 ~~during that taxable year if the corporation has made an election~~  
15 ~~pursuant to Section 170(a)(2) of the Internal Revenue Code,~~  
16 ~~relating to corporations on accrual basis, for federal income tax~~  
17 ~~purposes with respect to that contribution.~~

18 ~~(c) For purposes of this section, payment of a charitable~~  
19 ~~contribution that consists of a future interest in tangible personal~~  
20 ~~property shall be treated as made only when all intervening~~  
21 ~~interests in, and rights to the actual possession or enjoyment of, the~~  
22 ~~property have expired or are held by persons other than the~~  
23 ~~taxpayer or those standing in a relationship to the taxpayer~~  
24 ~~described in Section 24428. For purposes of the preceding~~  
25 ~~sentence, a fixture which is intended to be severed from the real~~  
26 ~~property shall be treated as tangible personal property.~~

27 ~~(d) No deduction shall be allowed under this section for~~  
28 ~~traveling expenses (including amounts expended for meals and~~  
29 ~~lodging) while away from home, whether paid directly or by~~  
30 ~~reimbursement, unless there is no significant element of personal~~  
31 ~~pleasure, recreation, or vacation in that travel.~~

32 ~~(e) (1) Section 170(f)(8) of the Internal Revenue Code,~~  
33 ~~relating to substantiation requirement for certain contributions,~~  
34 ~~shall apply, except as otherwise provided.~~

35 ~~(2) No deduction shall be denied under Section 170(f)(8) of the~~  
36 ~~Internal Revenue Code, relating to substantiation requirement for~~  
37 ~~certain contributions, upon a showing that the requirements in~~  
38 ~~Section 170(f)(8) of the Internal Revenue Code have been met~~  
39 ~~with respect to that contribution for federal purposes.~~

1 ~~SEC. 41.4.— Section 24362 of the Revenue and Taxation Code~~  
2 ~~is amended to read:~~

3 ~~24362.— Sections 24360 to 24363.5, inclusive, shall apply to~~  
4 ~~the bonds only if the taxpayer has made the election pursuant to~~  
5 ~~Section 171(e) of the Internal Revenue Code for federal income~~  
6 ~~tax purposes to have Section 171 of the Internal Revenue Code,~~  
7 ~~relating to amortizable bond premium, apply for federal income~~  
8 ~~tax purposes to the bonds.~~

9 ~~SEC. 41.6.— Section 24364 of the Revenue and Taxation Code~~  
10 ~~is amended to read:~~

11 ~~24364.— Notwithstanding Article 3 (commencing with Section~~  
12 ~~24421), all expenditures (other than expenditures for the purchase~~  
13 ~~of land or depreciable property or for the acquisition of circulation~~  
14 ~~through the purchase of any part of the business of another~~  
15 ~~publisher of a newspaper, magazine, or other periodical) to~~  
16 ~~establish, maintain, or increase the circulation of a newspaper,~~  
17 ~~magazine, or other periodical shall be allowed as a deduction.~~  
18 ~~However, the deduction shall not be allowed with respect to the~~  
19 ~~portion of the expenditures that the taxpayer has elected, pursuant~~  
20 ~~to Section 173 of the Internal Revenue Code, to treat as chargeable~~  
21 ~~to capital account for federal income tax purposes.~~

22 ~~SEC. 42.— Section 24369.4 of the Revenue and Taxation Code~~  
23 ~~is amended to read:~~

24 ~~24369.4.— (a) Section 198 of the Internal Revenue Code,~~  
25 ~~relating to expensing of environmental remediation costs, shall~~  
26 ~~apply, except as otherwise provided.~~

27 ~~(b) Section 198(b)(2) is modified to refer to Sections 24349 to~~  
28 ~~24355, inclusive, in lieu of Section 167 of the Internal Revenue~~  
29 ~~Code.~~

30 ~~(c) Section 198(f) is modified to refer to Section 24442 in lieu~~  
31 ~~of Section 280B of the Internal Revenue Code.~~

32 ~~(d) (1) If a taxpayer has, at any time, made an election for~~  
33 ~~federal income tax purposes under Section 198(a) of the Internal~~  
34 ~~Revenue Code to have Section 198 of the Internal Revenue Code~~  
35 ~~apply to a qualified environmental remediation expenditure,~~  
36 ~~Section 198 of the Internal Revenue Code shall apply to that~~  
37 ~~qualified environmental remediation expenditure for state~~  
38 ~~purposes, a separate election for state purposes shall not be~~  
39 ~~allowed and the federal election shall be binding for purposes of~~  
40 ~~this part.~~

1     ~~(2) If a taxpayer fails to make an election for federal income tax~~  
2 ~~purposes under Section 198(a) of the Internal Revenue Code to~~  
3 ~~have Section 198 of the Internal Revenue Code apply to a qualified~~  
4 ~~environmental remediation expenditure, an election under Section~~  
5 ~~198(a) of the Internal Revenue Code shall not be allowed for state~~  
6 ~~purposes, Section 198 of the Internal Revenue Code shall not apply~~  
7 ~~to that qualified environmental remediation expenditure for state~~  
8 ~~purposes, and a separate election for state purposes shall not be~~  
9 ~~allowed.~~

10     ~~(c) No inference as to the proper treatment for purposes of this~~  
11 ~~part of qualified environmental remediation expenditures for~~  
12 ~~periods before the enactment of this section shall be made.~~

13     ~~SEC. 42.2. Section 24377 of the Revenue and Taxation Code~~  
14 ~~is repealed.~~

15     ~~SEC. 42.4. Section 24377 is added to the Revenue and~~  
16 ~~Taxation Code, to read:~~

17     ~~24377. Section 180 of the Internal Revenue Code, relating to~~  
18 ~~expenditures by farmers for fertilizer, etc., shall apply, except as~~  
19 ~~otherwise provided.~~

20     ~~SEC. 42.6. Section 24407 of the Revenue and Taxation Code~~  
21 ~~is amended to read:~~

22     ~~24407. The organizational expenditures of a corporation shall~~  
23 ~~be treated as deferred expenses if the corporation has made an~~  
24 ~~election pursuant to Section 248 of the Internal Revenue Code for~~  
25 ~~federal income tax purposes with respect to those expenses. In~~  
26 ~~computing net income, the deferred expenses shall be allowed as~~  
27 ~~a deduction ratably over that period of not less than 60 months as~~  
28 ~~has been selected by the corporation (beginning with the month in~~  
29 ~~which the corporation begins business) for federal income tax~~  
30 ~~purposes pursuant to Section 248 of the Internal Revenue Code.~~

31     ~~SEC. 42.8. Section 24409 of the Revenue and Taxation Code~~  
32 ~~is amended to read:~~

33     ~~24409. The period that applies under Section 24407 shall be~~  
34 ~~adhered to in computing the income of the corporation for the~~  
35 ~~taxable year for which the election is made pursuant to Section 248~~  
36 ~~of the Internal Revenue Code for federal income tax purposes with~~  
37 ~~respect to those expenses and all subsequent taxable years.~~

38     ~~SEC. 43. Section 24423 of the Revenue and Taxation Code is~~  
39 ~~amended to read:~~



~~24423. (a) Notwithstanding Section 24422, regulations shall be prescribed by the Franchise Tax Board under this part corresponding to the regulations which granted the option to deduct as expenses intangible drilling and development costs in the case of oil and gas wells and which were recognized and approved by the Congress in House Concurrent Resolution 50, Seventy-ninth Congress.~~

~~(b) Section 263(i) of the Internal Revenue Code, relating to special rules for intangible drilling and development costs incurred outside the United States, shall apply, except as otherwise provided.~~

~~SEC. 43.2. Section 24426 of the Revenue and Taxation Code is amended to read:~~

~~24426. Amounts paid or accrued for such taxes and carrying charges as, pursuant to an election under Section 266 of the Internal Revenue Code for federal income tax purposes, are chargeable to capital account with respect to property.~~

~~SEC. 43.4. Section 24651 of the Revenue and Taxation Code is amended to read:~~

~~24651. (a) Income shall be computed under the method of accounting on the basis of which the taxpayer regularly computes its income in keeping its books and utilizes for federal income tax purposes if the taxpayer has a federal income tax filing requirement.~~

~~(b) If the taxpayer has no federal income tax filing requirement and no method of accounting has been regularly used by the taxpayer, or if the method used does not clearly reflect income, the computation of income shall be made under such method as, in the opinion of the Franchise Tax Board, does clearly reflect income.~~

~~(c) Subject to subdivisions (a) and (b) and Section 24654, a taxpayer may compute income under any of the following methods of accounting—~~

~~(1) The cash receipts and disbursements method;~~

~~(2) An accrual method;~~

~~(3) Any other method permitted by this part; or~~

~~(4) Any combination of the foregoing methods permitted under regulations prescribed by the Franchise Tax Board.~~

~~(d) A taxpayer engaged in more than one trade or business may in computing income, use a different method of accounting for each trade or business, but the method used shall be the same as the~~

method used for federal income tax purposes for that trade or business. If the trade or business is not subject to federal income tax, then the taxpayer shall use the method of accounting on the basis that the taxpayer regularly computes the income for that trade or business in keeping its books, subject to subdivision (b).

(e) Except as otherwise expressly provided in this part, a taxpayer who changes the method of accounting on the basis of which it regularly computes its income in keeping its books shall, before computing its income under the new method, secure the consent of the Franchise Tax Board. Any change in method of accounting granted or required for federal income tax purposes shall be binding for purposes of this part, and the change will apply automatically without the requirement for consent by the Franchise Tax Board. However, the Franchise Tax Board may make proper adjustments to any adjustments required by changes in accounting under Section 481 of the Internal Revenue Code and Section 24721. Adjustments computed under Section 481 of the Internal Revenue Code and Section 24721 shall take into account differences in federal and California law.

(f) If the taxpayer is required to and does not file with the Franchise Tax Board a request to change the method of accounting, the absence of the consent of the Franchise Tax Board to a change in the method of accounting shall not be taken into account for either of the following:

(1) To prevent the imposition of any penalty, or the addition of any amount to tax, under this part.

(2) To diminish the amount of that penalty or addition to tax.

SEC. 43.6. — Section 24674 of the Revenue and Taxation Code is amended to read:

24674. (a) If, in the case of a taxpayer owning any non-interest-bearing obligation issued at a discount and redeemable for fixed amounts increasing at stated intervals, the increase in the redemption price of the obligation occurring in the taxable year does not (under the method of accounting used in computing its income) constitute income to it in the taxable year, the taxpayer shall treat the increase as income received in the taxable year if the taxpayer has made an election pursuant to Section 454 of the Internal Revenue Code for federal tax purposes. If the preceding sentence applies with respect to any obligation described in that sentence, it shall also apply to all obligations

described in that sentence owned by the taxpayer at the beginning of the first taxable year to which it applies and to all obligations described in that sentence thereafter acquired by it and shall be binding for all subsequent taxable years that the taxpayer's election pursuant to Section 454 of the Internal Revenue Code remains in effect for federal income tax purposes.

(b) In the case of any obligation—

(1) Of the United States; or

(2) Of a state, a territory, or a possession of the United States, or any political subdivision of any of the foregoing, or of the District of Columbia, which is issued on a discount basis and payable without interest at a fixed maturity date not exceeding one year from the date of issue, the amount of discount at which such obligation is originally sold shall not be considered to accrue until the date on which such obligation is paid at maturity, sold, or otherwise disposed of.

SEC. 43.8.— Section 24676 of the Revenue and Taxation Code is repealed.

SEC. 44.— Section 24676 is added to the Revenue and Taxation Code, to read:

24676.— (a) Section 455 of the Internal Revenue Code, relating to prepaid subscription income, shall apply, except as otherwise provided.

(b) Section 455(b)(2) of the Internal Revenue Code is modified by substituting the phrase “If the taxpayer ceases to be subject to tax measured by net income imposed under Chapter 2 (commencing with Section 23101) or Chapter 3 (commencing with Section 23501) of this part” for the phrase “If the taxpayer dies or ceases to exist” contained therein.

(c) Section 455(b)(2) of the Internal Revenue Code is modified by substituting the phrase “shall be included in the measure of tax for the last year in which the taxpayer is subject to the tax measured by net income imposed under Chapter 2 (commencing with Section 23101) or Chapter 3 (commencing with Section 23501) of this part” for the phrase “shall be included in gross income for the taxable year in which such death, or such cessation of existence, occurs” contained therein.

SEC. 44.2.— Section 24676.5 of the Revenue and Taxation Code is repealed.

1 ~~SEC. 44.6. Section 24676.5 is added to the Revenue and~~  
2 ~~Taxation Code, to read:~~

3 ~~24676.5. (a) Section 458 of the Internal Revenue Code,~~  
4 ~~relating to magazines, paperbacks, and records returned after the~~  
5 ~~close of the taxable year, shall apply, except as otherwise provided.~~

6 ~~(b) Section 458(d) of the Internal Revenue Code is modified by~~  
7 ~~substituting “Section 24723” for “section 481(e)” and~~  
8 ~~“subdivision (b) of Section 24721” and “section 481(a)(2).”~~

9 ~~(c) Section 458(e)(1) of the Internal Revenue Code is modified~~  
10 ~~by substituting “Sections 24721 to 24725, inclusive,” for~~  
11 ~~“section 481.”~~

12 ~~SEC. 44.8. Section 24710 of the Revenue and Taxation Code~~  
13 ~~is amended to read:~~

14 ~~24710. (a) For each taxable year beginning on or after~~  
15 ~~January 1, 1997, Section 475 of the Internal Revenue Code,~~  
16 ~~relating to mark to market accounting method for securities~~  
17 ~~dealers, shall apply, except as otherwise provided.~~

18 ~~(b) Section 13233(e)(2)(C) of the Revenue Reconciliation Act~~  
19 ~~of 1993 (Public Law 103-66), relating to the effective date for~~  
20 ~~changes in the mark to market accounting method for securities~~  
21 ~~dealers, is modified to provide that the amount taken into account~~  
22 ~~under Section 481 of the Internal Revenue Code of 1986 shall be~~  
23 ~~taken into account ratably over the five taxable year period~~  
24 ~~beginning with the first taxable year beginning on or after January~~  
25 ~~1, 1997.~~

26 ~~(c) (1) If a taxpayer has, at any time, made an election for~~  
27 ~~federal income tax purposes under Section 475(e) of the Internal~~  
28 ~~Revenue Code, relating to election of mark to market for dealers~~  
29 ~~in commodities, to have Section 475 of the Internal Revenue Code~~  
30 ~~apply, Section 475 of the Internal Revenue Code shall apply to that~~  
31 ~~dealer in commodities for state purposes, a separate election for~~  
32 ~~state purposes shall not be allowed and the federal election shall~~  
33 ~~be binding for purposes of this part.~~

34 ~~(2) If a taxpayer fails to make, or has not previously made, an~~  
35 ~~election for federal income tax purposes under Section 475(e) of~~  
36 ~~the Internal Revenue Code, relating to election of mark to market~~  
37 ~~for dealers in commodities, to have Section 475 of the Internal~~  
38 ~~Revenue Code apply, an election under Section 475(e) of the~~  
39 ~~Internal Revenue Code shall not be allowed for state purposes,~~  
40 ~~Section 475 of the Internal Revenue Code shall not apply to that~~

1 dealer in commodities for state purposes, and a separate election  
2 for state purposes shall not be allowed.

3 (d) (1) If a taxpayer has, at any time, made an election for  
4 federal income tax purposes under Section 475(f)(1) of the  
5 Internal Revenue Code, relating to election of mark to market for  
6 traders in securities, to have Section 475 of the Internal Revenue  
7 Code apply to a trade or business, Section 475 of the Internal  
8 Revenue Code shall apply to that trader in securities for state  
9 purposes with respect to that trade or business, a separate election  
10 for state purposes with respect to that trade or business shall not be  
11 allowed and the federal election shall be binding for purposes of  
12 this part.

13 (2) If a taxpayer fails to make, or has not previously made, an  
14 election for federal income tax purposes under Section 475(f)(1)  
15 of the Internal Revenue Code, relating to election of mark to  
16 market for traders in securities, to have Section 475 of the Internal  
17 Revenue Code apply to a trade or business, an election under  
18 Section 475(f)(1) of the Internal Revenue Code shall not be  
19 allowed for state purposes with respect to that trade or business,  
20 Section 475 of the Internal Revenue Code shall not apply to that  
21 trader in securities for state purposes with respect to that trade or  
22 business, and a separate election for state purposes shall not be  
23 allowed.

24 (e) (1) If a taxpayer has, at any time, made an election for  
25 federal income tax purposes under Section 475(f)(2) of the  
26 Internal Revenue Code, relating to election of mark to market for  
27 traders in commodities, to have Section 475 of the Internal  
28 Revenue Code apply to a trade or business, Section 475 of the  
29 Internal Revenue Code shall apply to that trader in commodities  
30 for state purposes with respect to that trade or business, a separate  
31 election for state purposes with respect to that trade or business  
32 shall not be allowed and the federal election with respect to that  
33 trade or business shall be binding for purposes of this part.

34 (2) If a taxpayer fails to make, or has not previously made, an  
35 election for federal income tax purposes under Section 475(f)(2)  
36 of the Internal Revenue Code, relating to election of mark to  
37 market for traders in commodities, to have Section 475 of the  
38 Internal Revenue Code apply to a trade or business, an election  
39 under Section 475(f)(2) of the Internal Revenue Code shall not be  
40 allowed for state purposes with respect to that trade or business,

Section 475 of the Internal Revenue Code shall not apply to that trader in commodities for state purposes with respect to that trade or business, and a separate election for state purposes with respect to that trade or business shall not be allowed.

(f) (1) An election under Section 475(c) or (f) of the Internal Revenue Code made for federal income tax purposes with respect to a taxable year beginning before January 1, 1998, shall be treated as having been made for state purposes with respect to the first taxable year beginning on or after January 1, 1998.

(2) Section 1001(d)(4)(B) of the Taxpayer Relief Act of 1997 (Public Law 105-34), relating to the effective date for election of mark to market by securities traders and traders and dealers in commodities, is modified to provide that the requirement for timely identification shall be treated as timely made for state purposes if that identification is treated as timely made for federal income tax purposes, and the amount taken into account under Section 481 of the Internal Revenue Code of 1986 shall be taken into account ratably over the four-taxable-year period beginning with the first taxable year beginning on or after January 1, 1998.

SEC. 45.—Section 24872.4 of the Revenue and Taxation Code is amended to read:

24872.4. (a) Section 856(d)(7)(C)(ii) of the Internal Revenue Code is modified by substituting the phrase “if received by an organization described in subdivision (b) of Section 17651 of Part 10 or Section 23731” for the phrase “if received by an organization described in section 511(a)(2).”

(b) (1) An election under Section 856(e)(5) of the Internal Revenue Code for federal income tax purposes shall be treated for purposes of this part as an election made by the real estate investment trust under Section 856(e)(5) of the Internal Revenue Code for state purposes and a separate election shall not be allowed.

(2) Any revocation of an election under Section 856(e)(5) of the Internal Revenue Code for federal income tax purposes shall be treated for purposes of this part as a revocation of the election made by the real estate investment trust under Section 856(e)(5) of the Internal Revenue Code for state purposes and a separate election shall not be allowed with respect to the property for any subsequent taxable year.

~~(3) If the real estate investment trust fails to make an election under Section 856(e)(5) of the Internal Revenue Code for federal income tax purposes with respect to any property, that property shall not be treated for purposes of this part as foreclosure property, an election under Section 856(e)(5) of the Internal Revenue Code for state purposes with respect to that property shall not be allowed, and a separate election shall not be allowed with respect to that property.~~

~~(c) This section shall apply to taxable years beginning after August 5, 1997.~~

~~(d) The amendments made to this section by the act adding this subdivision shall apply to taxable years beginning on or after January 1, 1998.~~

~~SEC. 46. Section 24944 of the Revenue and Taxation Code is amended to read:~~

~~24944. If property (as a result of its destruction in whole or in part, theft, seizure, or requisition or condemnation or threat or imminence thereof) is compulsorily or involuntarily converted into money or into property not similar or related in service or use to the converted property, and the disposition of the converted property (as defined in subdivision (b) of Section 24943) occurred after December 31, 1952, the gain (if any) shall be recognized except to the extent hereinafter provided in this section:~~

~~(a) If the taxpayer during the period specified in subdivision (b), for the purpose of replacing the property so converted, purchases other property similar or related in service or use to the property so converted, or purchases stock in the acquisition of control of a corporation owning replacement property and the taxpayer has made an election pursuant to Section 1033(a)(2)(A) of the Internal Revenue Code for federal income tax purposes, the gain shall be recognized only to the extent that the amount realized upon the conversion (regardless of whether that amount is received in one or more taxable years) exceeds the cost of the replacement property or stock. For purposes of this subdivision—~~

~~(1) No property or stock acquired before the disposition of the converted property shall be considered to have been acquired for the purpose of replacing the converted property unless held by the taxpayer on the date of such disposition; and~~

~~(2) The taxpayer shall be considered to have purchased property or stock only if, but for the provisions of Section 24947,~~



1 the unadjusted basis of the replacement property or stock would be  
2 its cost within the meaning of Section 24912.

3 (b) The period referred to in subdivision (a) shall be the period  
4 beginning with the date of the disposition of the converted  
5 property, or the earliest date of the threat or imminence of  
6 requisition or condemnation of the converted property, whichever  
7 is the earlier, and ending—

8 (1) Two years after the close of the first taxable year in which  
9 any part of the gain upon the conversion is realized; or

10 (2) Subject to any terms and conditions as may be specified by  
11 the Franchise Tax Board, at the close of a later date as the Franchise  
12 Tax Board may designate on application by the taxpayer. The  
13 application shall be made at the time and in manner as the  
14 Franchise Tax Board may prescribe.

15 (c) For purposes of this section and Section 24943,  
16 replacement property “similar or related in service or use” shall  
17 include, in the case of a nonprofit water utility corporation,  
18 personal property used for the transmission or storage of water.

19 SEC. 47.— Section 24946 of the Revenue and Taxation Code is  
20 amended to read:

21 24946.— If subdivision (a) of Section 24944 applies to the  
22 taxpayer, and the replacement property or stock was purchased  
23 before the beginning of the last taxable year in which any part of  
24 the gain upon the conversion is realized, any deficiency, to the  
25 extent resulting from the application of subdivision (a) of Section  
26 24944, for any taxable year ending before that last taxable year  
27 may be assessed (notwithstanding the provisions of Section 19057  
28 or the provisions of any other law or rule of law which would  
29 otherwise prevent the assessment) at any time before the  
30 expiration of the period within which a deficiency for that last  
31 taxable year may be assessed.

32 SEC. 48.— Section 24949.2 of the Revenue and Taxation Code  
33 is amended to read:

34 24949.2.— (a) For purposes of Sections 24943 through 24945,  
35 if real property (not including stock in trade or other property held  
36 primarily for sale) held for productive use in trade or business or  
37 for investment is (as a result of its seizure, requisition, or  
38 condemnation, or threat or imminence thereof) compulsorily or  
39 involuntarily converted, property of a like kind to be held either  
40 for productive use in trade or business or for investment shall be

1 ~~treated as property similar or related in service or use to the~~  
2 ~~property so converted.~~

3 ~~(b) (1) Subdivision (a) shall not apply to the purchase of stock~~  
4 ~~in the acquisition of control of a corporation described in~~  
5 ~~subdivision (a) of Section 24944.~~

6 ~~(2) Subdivision (a) shall apply with respect to the compulsory~~  
7 ~~or involuntary conversion of any real property only if the~~  
8 ~~disposition of the converted property (within the meaning of~~  
9 ~~subdivision (b) of Section 24943) occurs after December 31, 1960.~~

10 ~~(c) (1) A taxpayer may elect, at such time and in such manner~~  
11 ~~as the Franchise Tax Board may prescribe, to treat property which~~  
12 ~~constitutes an outdoor advertising display as real property for~~  
13 ~~purposes of this part with respect to which an election under~~  
14 ~~Section 24356.6, 24356.7, or 24356.8 (relating to election to~~  
15 ~~expense certain depreciable business assets) is in effect.~~

16 ~~(2) An election made under paragraph (1) may not be revoked~~  
17 ~~without the consent of the Franchise Tax Board.~~

18 ~~(3) For purposes of this subdivision, the term “outdoor~~  
19 ~~advertising display” means a rigidly assembled sign, display, or~~  
20 ~~device permanently affixed to the ground or permanently attached~~  
21 ~~to a building or other inherently permanent structure constituting,~~  
22 ~~or used for the display of, a commercial or other advertisement to~~  
23 ~~the public.~~

24 ~~(4) For purposes of this subdivision, an interest in real property~~  
25 ~~purchased as replacement property for a compulsorily or~~  
26 ~~involuntarily converted outdoor advertising display defined in~~  
27 ~~paragraph (3) (and treated by the taxpayer as real property) shall~~  
28 ~~be considered property of a like kind as the property converted~~  
29 ~~without regard to whether the taxpayer’s interest in the~~  
30 ~~replacement property is the same kind of interest the taxpayer held~~  
31 ~~in the converted property.~~

32 ~~(d) In the case of a compulsory or involuntary conversion~~  
33 ~~described in subdivision (a), paragraph (1) of subdivision (b) of~~  
34 ~~Section 24944 shall be applied by substituting “three years” for~~  
35 ~~“two years.”~~

36 ~~(e) Subdivision (d) shall apply with respect to any disposition~~  
37 ~~of converted property (within the meaning of Section 24944) after~~  
38 ~~December 31, 1976.~~

39 ~~SEC. 49. (a) Except for the changes made by this act to~~  
40 ~~Section 23801 of the Revenue and Taxation Code that require a~~

1 corporation that has in effect for federal income tax purposes a  
2 valid election under Section 1362(a) of the Internal Revenue Code  
3 to be an S corporation for purposes of Part 10 (commencing with  
4 Section 17001), Part 10.2 (commencing with Section 18401), and  
5 Part 11 (commencing with Section 23001) of the Revenue and  
6 Taxation Code, it is the intent of the Legislature that this act not be  
7 construed in a manner that would require any taxpayer that has  
8 made, or has in effect, a valid separate state election or a valid  
9 separate state method of accounting to change that election or  
10 method to be the same as that taxpayer's election or method for  
11 federal income tax purposes. The preceding sentence shall only  
12 apply to any election or method that has been made or is in effect  
13 for taxable years beginning before January 1, 2002.

14 (b) (1) A taxpayer that has made, or has in effect, a valid  
15 separate state election or a valid separate state method of  
16 accounting under Sections 17024.5 or 23051.5 of the Revenue and  
17 Taxation Code, as in effect for taxable years beginning before  
18 January 1, 2002, may, in the form and manner in which the  
19 Franchise Tax Board may specify in forms and instructions, elect  
20 or otherwise apply to the Franchise Tax Board for consent under  
21 this subdivision to have that taxpayer's federal election or federal  
22 method of accounting apply for purposes of Part 10 (commencing  
23 with Section 17001), Part 10.2 (commencing with Section 18401),  
24 or Part 11 (commencing with Section 23001) of the Revenue and  
25 Taxation Code.

26 (2) In the case of any taxpayer making the election or  
27 application for consent allowed under paragraph (1) to apply the  
28 taxpayer's federal election or method of accounting for any  
29 taxable year beginning on or after January 1, 2002, for purposes  
30 of Part 10 (commencing with Section 17001), Part 10.2  
31 (commencing with Section 18401), or Part 11 (commencing with  
32 Section 23001) of the Revenue and Taxation Code, the following  
33 rules shall apply to that election or application for consent:

34 (a) The change shall be treated as initiated by the taxpayer.

35 (b) The change shall be treated as made with the consent of the  
36 Franchise Tax Board.

37 (c) The net amount of the adjustments required to be taken into  
38 account under Section 481 of the Internal Revenue Code, as  
39 applicable for purposes of Part 10 (commencing with Section  
40 17001) or Part 11 (commencing with Section 23001) of the

1 ~~Revenue and Taxation Code, shall be taken into account ratably~~  
2 ~~over the four-taxable year period beginning with the first taxable~~  
3 ~~year for which the election or application for consent is effective~~  
4 ~~under this subdivision.~~

5 ~~SEC. 50.—~~

6 *SEC. 44. Section 24357.9 of the Revenue and Taxation Code*  
7 *is amended to read:*

8 24357.9. (a) In the case of a qualified ~~elementary or~~  
9 ~~secondary educational computer~~ contribution, the amount  
10 otherwise allowed as a deduction under Section 24357 shall be  
11 reduced by that amount of the reduction provided by Section  
12 24357.1 which is no greater than the sum of the following:

13 (1) One-half of the amount computed pursuant to Section  
14 24357.1 (computed without regard to this paragraph).

15 (2) The amount (if any) by which the charitable contribution  
16 deduction under this section for any qualified elementary or  
17 secondary educational contribution (computed by taking into  
18 account the amount determined by paragraph (1), but without  
19 regard to this paragraph) exceeds twice the basis of the property.

20 (b) For purposes of this section, the term “qualified ~~elementary~~  
21 ~~or secondary educational computer~~ contribution” means a  
22 charitable contribution by a corporation of any computer  
23 technology or equipment, but only if all of the following apply:

24 (1) The contribution is to either of the following:

25 (A) An educational organization described in Section  
26 170(b)(1)(A)(ii) of the Internal Revenue Code.

27 (B) An entity described in Section 23701d and exempt from tax  
28 under Section 23701 (other than an entity described in  
29 subparagraph (A)) that is organized primarily for purposes of  
30 supporting elementary and secondary education in California.

31 (C) A *public library (as described in Section*  
32 *170(e)(6)(B)(i)(III) of the Internal Revenue Code.*

33 (2) The contribution is made not later than ~~two~~ *three* years after  
34 the date the taxpayer acquired the property (or in the case of  
35 property constructed by the taxpayer, the date the construction of  
36 the property is substantially completed).

37 (3) The original use of the property is by the donor or the donee.

38 (4) Substantially all of the use of the property by the donee is  
39 for use within California for educational purposes in any of the

1 grades K through 12 that are related to the purpose or function of  
2 the organization or entity.

3 (5) The property is not transferred by the donee in exchange for  
4 money, other property, or services, except for shipping,  
5 installation, and transfer of costs.

6 (6) The property will fit productively into the entity's  
7 educational plan.

8 (7) The entity's use and disposition of the property will be in  
9 accordance with paragraphs (4) and (5).

10 (8) *The property meets the standards, if any, as the Secretary of*  
11 *the Treasury may have prescribed by regulation under Section*  
12 *170(e)(6) of the Internal Revenue Code to assure that the property*  
13 *meets minimum functionality and suitability standards for*  
14 *educational purposes.*

15 (c) A contribution by a corporation of any computer  
16 technology or equipment to a private foundation (as defined in  
17 Section 509 of the Internal Revenue Code) shall be treated as a  
18 qualified ~~elementary or secondary educational~~ computer  
19 contribution for purposes of this section if both of the following  
20 apply:

21 (1) The contribution to the private foundation satisfies the  
22 requirements of paragraphs (2) and (5) of subdivision (b).

23 (2) Within 30 days after that contribution, the private  
24 foundation does both of the following:

25 (A) Contributes the property to an entity described in  
26 paragraph (1) of subdivision (b) that satisfies the requirements of  
27 paragraphs (4) to (7), inclusive, of subdivision (b).

28 (B) Notifies the donor of that contribution.

29 (d) *In the case of property which is reacquired by the person*  
30 *who constructed the property, both of the following shall apply:*

31 (1) *Paragraph (2) of subdivision (b) shall be applied to a*  
32 *contribution of that property by that person by taking into account*  
33 *the date that the original construction of the property was*  
34 *substantially completed.*

35 (2) *Paragraph (3) of subdivision (b) shall not apply to that*  
36 *contribution.*

37 (e) For purposes of this section, property shall be treated as  
38 constructed by the taxpayer only if the cost of the parts used in the  
39 construction of that property (other than parts manufactured by the

1 taxpayer or a related person) do not exceed 50 percent of the  
2 taxpayer's basis in that property.

3 ~~(e)~~

4 (f) For purposes of this section:

5 (1) "Computer technology or equipment" means computer  
6 software (as defined by Section 197(e)(3)(B) of the Internal  
7 Revenue Code), computer or peripheral equipment (as defined by  
8 Section 168(i)(2)(B) of the Internal Revenue Code), and  
9 fiber-optic cable related to computer use.

10 (2) "Corporation" shall not include any of the following:

11 (A) An "S corporation."

12 (B) A personal holding company (as defined in Section 542 of  
13 the Internal Revenue Code).

14 (C) A service organization (as defined in Section 414(m)(3) of  
15 the Internal Revenue Code).

16 ~~(f)~~

17 (g) (1) This section shall not apply to any contribution made  
18 during any taxable year beginning on or after January 1, 2000, and  
19 before December 31, 2001.

20 (2) This section shall not apply to any contribution made  
21 during any taxable year beginning after December 31, 2003.

22 SEC. 45. Section 24424 of the Revenue and Taxation Code is  
23 amended to read:

24 24424. ~~(a) No deduction shall be allowed for—~~

25 ~~(1) Premiums paid on any life insurance policy, or endowment~~  
26 ~~or annuity contract, if the taxpayer is directly or indirectly a~~  
27 ~~beneficiary under that policy or contract.~~

28 ~~(2) Any amount paid or accrued on indebtedness incurred to~~  
29 ~~purchase or carry a single premium life insurance, endowment, or~~  
30 ~~annuity contract. This paragraph shall apply with respect to~~  
31 ~~annuity contracts only as to contracts purchased after December~~  
32 ~~31, 1954.~~

33 ~~(3) Except as provided in subdivision (c), any amount paid or~~  
34 ~~accrued on indebtedness incurred or continued to purchase or carry~~  
35 ~~a life insurance, endowment, or annuity contract (other than a~~  
36 ~~single premium contract or a contract treated as a single premium~~  
37 ~~contract) pursuant to a plan of purchase which contemplates the~~  
38 ~~systematic direct or indirect borrowing of part or all of the~~  
39 ~~increases in the cash value of that contract (either from the insurer~~

1 ~~or otherwise). This paragraph shall apply only with respect to~~  
2 ~~contracts purchased after August 6, 1963.~~

3 ~~(4) Except as provided in subdivision (d), any interest paid or~~  
4 ~~accrued on any indebtedness with respect to one or more insurance~~  
5 ~~policies owned by the taxpayer covering the life of any individual,~~  
6 ~~or any endowment or annuity contracts owned by the taxpayer~~  
7 ~~covering any individual.~~

8 ~~This paragraph shall apply with respect to contracts purchased~~  
9 ~~after June 20, 1986.~~

10 ~~(b) Paragraph (1) of subdivision (a) shall not apply to either of~~  
11 ~~the following:~~

12 ~~(1) Any annuity contract described in Section 72(s)(5) of the~~  
13 ~~Internal Revenue Code.~~

14 ~~(2) Any annuity contract to which Section 72(u) of the Internal~~  
15 ~~Revenue Code applies.~~

16 ~~(c) For purposes of paragraph (2) of subdivision (a), a contract~~  
17 ~~shall be treated as a single premium contract if either of the~~  
18 ~~following conditions exist:~~

19 ~~(1) Substantially all the premiums on the contract are paid~~  
20 ~~within a period of four years from the date on which the contract~~  
21 ~~is purchased.~~

22 ~~(2) An amount is deposited after December 31, 1954, with the~~  
23 ~~insurer for payment of a substantial number of future premiums on~~  
24 ~~the contract.~~

25 ~~(d) Paragraph (3) of subdivision (a) shall not apply to any~~  
26 ~~amount paid or accrued by a person during a taxable year on~~  
27 ~~indebtedness incurred or continued as part of a plan referred to in~~  
28 ~~paragraph (3) of subdivision (a) if any of the following is~~  
29 ~~applicable:~~

30 ~~(1) No part of four of the annual premiums due during the~~  
31 ~~seven-year period (beginning with the date the first premium on~~  
32 ~~the contract to which that plan relates was paid) is paid under that~~  
33 ~~plan by means of indebtedness.~~

34 ~~(2) The total of the amounts paid or accrued by that person~~  
35 ~~during that taxable year for which (without regard to this~~  
36 ~~paragraph) no deduction would be allowable by reason of~~  
37 ~~paragraph (3) of subdivision (a) does not exceed one hundred~~  
38 ~~dollars (\$100).~~



~~(3) That amount was paid or accrued on indebtedness incurred because of an unforeseen substantial loss of income or unforeseen substantial increase in its financial obligations.~~

~~(4) That indebtedness was incurred in connection with its trade or business.~~

~~For purposes of applying paragraph (1), if there is a substantial increase in the premiums on a contract, a new seven-year period described in that paragraph with respect to that contract shall commence on the date the first increased premium is paid.~~

~~(c) (1) Paragraph (4) of subdivision (a) shall not apply to any interest paid or accrued on any indebtedness with respect to policies or contracts covering an individual who is a key person to the extent that the aggregate amount of that indebtedness with respect to policies and contracts covering that individual does not exceed fifty thousand dollars (\$50,000).~~

~~(2) (A) No deduction shall be allowed by reason of paragraph (1) or the last sentence of subdivision (a) with respect to interest paid or accrued for any month beginning after December 31, 1995, to the extent the amount of that interest exceeds the amount which would have been determined if the applicable rate of interest were used for that month.~~

~~(B) For purposes of subparagraph (A):~~

~~(i) The applicable rate of interest for any month is the rate of interest described as Moody's Corporate Bond Yield Average Monthly Average Corporates, as published by Moody's Investors Service, Inc., or any successor thereto, for that month.~~

~~(ii) In the case of indebtedness on a contract purchased on or before June 20, 1986, all of the following shall apply:~~

~~(I) If the contract provides a fixed rate of interest, the applicable rate of interest for any month shall be the Moody's rate described in clause (i) for the month in which the contract was purchased.~~

~~(II) If the contract provides a variable rate of interest, the applicable rate of interest for any month in an applicable period shall be the Moody's rate described in clause (i) for the third month preceding the first month in that period.~~

~~(III) For purposes of subclause (II), the term "applicable period" means the 12-month period beginning on the date the policy is issued (and each successive 12-month period thereafter) unless the taxpayer elects a number of months (not greater than 12) other than that 12-month period to be its applicable period. That~~

1 election shall be made not later than the 90th day after the date of  
2 the enactment of the act adding this sentence and, if made, shall  
3 apply to the taxpayer's first taxable year ending on or after  
4 December 31, 1995, and all subsequent taxable years, unless  
5 revoked with the consent of the Franchise Tax Board.

6 (3) For purposes of paragraph (1), "key person" means an  
7 officer or 20 percent owner, except that the number of individuals  
8 who may be treated as key persons with respect to any taxpayer  
9 shall not exceed the greater of:

10 (A) Five individuals.

11 (B) The lesser of 5 percent of the total officers and employees  
12 of the taxpayer or 20 individuals.

13 (4) For purposes of this subdivision, "20-percent owner"  
14 means both of the following:

15 (A) If the taxpayer is a corporation, any person who directly  
16 owns 20 percent or more of the outstanding stock of the  
17 corporation or stock possessing 20 percent or more of the total  
18 combined voting power of all stock of the corporation.

19 (B) If the taxpayer is not a corporation, any person who owns  
20 20 percent or more of the capital or profits interest in the taxpayer.

21 (5) (A) For purposes of subparagraph (A) of paragraph (4) and  
22 for purposes of applying the fifty thousand dollars (\$50,000)  
23 limitation in paragraph (1) both of the following shall apply:

24 (i) All members of a controlled group shall be treated as one  
25 taxpayer.

26 (ii) The limitation shall be allocated among the members of the  
27 controlled group in the manner the Franchise Tax Board may  
28 prescribe.

29 (B) For purposes of this paragraph, all persons treated as a  
30 single employer under Section 52(a) or 52(b) of the Internal  
31 Revenue Code, relating to special rules, or Section 414(m) or  
32 414(o) of the Internal Revenue Code, relating to definitions and  
33 special rules, shall be treated as members of a controlled group.

34 (f) (1) No deduction shall be allowed for that portion of the  
35 taxpayer's interest expense which is allocable to unborrowed  
36 policy cash values.

37 (2) For purposes of paragraph (1), the portion of the taxpayer's  
38 interest expense which is allocable to unborrowed policy cash  
39 values is an amount which bears the same ratio to the interest  
40 expense as:

~~(A) The taxpayer's average unborrowed policy cash values of life insurance policies, and annuity and endowment contracts, issued after June 8, 1997, bears to~~

~~(B) The sum of:~~

~~(i) In the case of assets of the taxpayer which are life insurance policies or annuity or endowment contracts, the average unborrowed policy cash values of those policies and contracts, and~~

~~(ii) In the case of assets of the taxpayer not described in clause (i), the average adjusted bases (within the meaning of Section 24916) of those assets.~~

~~(3) For purposes of this subdivision, the term "unborrowed policy cash value" means, with respect to any life insurance policy or annuity or endowment contract, the excess of:~~

~~(A) The cash surrender value of the policy or contract determined without regard to any surrender charge, over~~

~~(B) The amount of any loan with respect to that policy or contract.~~

~~(4) (A) Paragraph (1) shall not apply to any policy or contract owned by an entity engaged in a trade or business if the policy or contract covers only one individual and if that individual is (at the time first covered by the policy or contract):~~

~~(i) A 20-percent owner of the entity, or~~

~~(ii) An individual (not described in clause (i)) who is an officer, director, or employee of that trade or business.~~

~~A policy or contract covering a 20-percent owner of the entity shall not be treated as failing to meet the requirements of the preceding sentence by reason of covering the joint lives of the owner and the owner's spouse.~~

~~(B) Paragraph (1) shall not apply to any annuity contract to which Section 72(u) of the Internal Revenue Code applies.~~

~~(C) Any policy or contract to which paragraph (1) does not apply by reason of this paragraph shall not be taken into account under paragraph (2).~~

~~(D) For purposes of subparagraph (A), the term "20-percent owner" has the meaning given such term by paragraph (4) of subdivision (e).~~

~~(5) (A) (i) This subdivision shall not apply to any policy or contract held by a natural person.~~

1     (ii) If a trade or business is directly or indirectly the beneficiary  
2 under any policy or contract, the policy or contract shall be treated  
3 as held by that trade or business and not by a natural person.

4     (iii) (I) Clause (ii) shall not apply to any trade or business  
5 carried on as a sole proprietorship and to any trade or business  
6 performing services as an employee.

7     (H) The amount of the unborrowed cash value of any policy or  
8 contract which is taken into account by reason of clause (ii) shall  
9 not exceed the benefit to which the trade or business is directly or  
10 indirectly entitled under the policy or contract.

11     (iv) A copy of the report required for federal purposes under  
12 Section 264(f) of the Internal Revenue Code shall be filed with the  
13 Franchise Tax Board at a time and in the manner specified for  
14 federal purposes and shall be treated as a statement referred to in  
15 Section 6724(d)(1) of the Internal Revenue Code.

16     (B) In the case of a partnership or S corporation, this  
17 subdivision shall be applied at the partnership and corporate  
18 levels.

19     (6) (A) If interest on any indebtedness is disallowed under  
20 subdivision (a) or Section 24425, both of the following shall apply:

21     (i) The disallowed interest shall not be taken into account for  
22 purposes of applying this subdivision.

23     (ii) The amount otherwise taken into account under  
24 subparagraph (B) of paragraph (2) shall be reduced (but not below  
25 zero) by the amount of the indebtedness.

26     (B) This subdivision shall be applied before the application of  
27 Section 263A of the Internal Revenue Code, relating to  
28 capitalization of certain expenses where taxpayer produces  
29 property.

30     (7) The term “interest expense” means the aggregate amount  
31 allowable to the taxpayer as a deduction for interest (within the  
32 meaning of Section 24344) for the taxable year (determined  
33 without regard to this subdivision, Section 24425, and Section 291  
34 of the Internal Revenue Code).

35     (8) All members of a controlled group (within the meaning of  
36 subparagraph (B) of paragraph (5) of subdivision (c)) shall be  
37 treated as one taxpayer for purposes of this subdivision.

38     (g) (1) The amendments made to this section by the act adding  
39 this subdivision shall apply to interest paid or accrued after  
40 December 31, 1995.

~~(2) (A) The amendments made to this section by the act adding this subdivision shall not apply to qualified interest paid or accrued on that indebtedness after December 31, 1995, and before January 1, 1999, in the case of either of the following:~~

~~(i) Indebtedness incurred before January 1, 1996.~~

~~(ii) Indebtedness incurred before January 1, 1997, with respect to any contract or policy entered into in 1994 or 1995.~~

~~(B) For purposes of subparagraph (A), the qualified interest with respect to any indebtedness for any month is the amount of interest (otherwise deductible) which would be paid or accrued for that month on that indebtedness if —~~

~~(i) In the case of any interest paid or accrued after December 31, 1995, indebtedness with respect to no more than 20,000 insured individuals were taken into account, and~~

~~(ii) The lesser of the following rates of interest were used for that month:~~

~~(I) The rate of interest specified under the terms of the indebtedness as in effect on December 31, 1995 (and without regard to modification of the terms after that date).~~

~~(II) The applicable percentage of the rate of interest described as Moody's Corporate Bond Yield Average Monthly Average Corporates as published by Moody's Investors Service, Inc., or any successor thereto, for that month. For purposes of clause (i), all persons treated as a single employer under Section 52(a) or 52(b) of the Internal Revenue Code, relating to special rules, or Section 414(m) or 414(o) of the Internal Revenue Code, relating to definitions and special rules, shall be treated as one person. Subclause (II) of clause (ii) shall not apply to any month before January 1, 1996.~~

~~(C) For purposes of subparagraph (B), the applicable percentage is as follows:~~

<del>For calendar year:</del>	<del>The percentage is:</del>
<del>—1996 —</del>	<del>100 percent —</del>
<del>—1997 —</del>	<del>90 percent —</del>
<del>—1998 —</del>	<del>80 percent —</del>

~~(3) This subdivision shall not apply to any contract purchased on or before June 20, 1986, except that paragraph (2) of~~

1 ~~subdivision (d) shall apply to interest paid or accrued after~~  
2 ~~December 31, 1995.~~

3 ~~(h) (1) Any amount received under any life insurance policy~~  
4 ~~or endowment or annuity contract described in paragraph (4) of~~  
5 ~~subdivision (a) shall be includable in gross income (in lieu of any~~  
6 ~~other inclusion in gross income) ratably over the four-taxable-year~~  
7 ~~period beginning with the taxable year that amount would (but for~~  
8 ~~this paragraph) be includable, upon the occurrence of either of the~~  
9 ~~following:~~

10 ~~(A) The complete surrender, redemption, or maturity of that~~  
11 ~~policy or contract during calendar year 1996, 1997, or 1998.~~

12 ~~(B) The full discharge during calendar year 1996, 1997, or~~  
13 ~~1998 of the obligation under the policy or contract which is in the~~  
14 ~~nature of a refund of the consideration paid for the policy or~~  
15 ~~contract.~~

16 ~~(2) Paragraph (1) shall only apply to the extent the amount is~~  
17 ~~includable in gross income for the taxable year in which the event~~  
18 ~~described in subparagraph (A) or (B) of paragraph (1) occurs.~~

19 ~~(3) Solely by reason of an occurrence described in~~  
20 ~~subparagraph (A) or (B) of paragraph (1) or solely by reason of no~~  
21 ~~additional premiums being received under the contract by reason~~  
22 ~~of a lapse occurring after December 31, 1995, a contract shall not~~  
23 ~~be treated as either of the following:~~

24 ~~(A) Failing to meet the requirement of paragraph (1) of~~  
25 ~~subdivision (c).~~

26 ~~(B) A single premium contract under paragraph (1) of~~  
27 ~~subdivision (b).~~

28 ~~(i) The amendments made by the act adding this subdivision~~  
29 ~~shall apply to contracts issued after June 8, 1997, in taxable years~~  
30 ~~beginning on or after January 1, 1998. For purposes of the~~  
31 ~~preceding sentence, any material increase in the death benefit or~~  
32 ~~other material change in the contract shall be treated as a new~~  
33 ~~contract, except that the addition of covered lives shall be treated~~  
34 ~~as a new contract only with respect to those additional covered~~  
35 ~~lives. For purposes of this subdivision, an increase in the death~~  
36 ~~benefit under a policy of contract issued in connection with a lapse~~  
37 ~~described in Section 501(d)(2) of the Health Insurance Portability~~  
38 ~~and Accountability Act of 1996 shall not be treated as a new~~  
39 ~~contract. Section 264 of the Internal Revenue Code, relating to~~

1 certain amounts paid in connection with insurance contracts, shall  
2 apply, except as otherwise provided.

3 SEC. 46. Section 24443 of the Revenue and Taxation Code is  
4 amended to read:

5 24443. ~~(a)~~ Section 274 of the Internal Revenue Code,  
6 relating to the disallowance of certain entertainment, gift, travel,  
7 etc., expenses, shall apply, except as otherwise provided.

8 ~~(b) Section 274(a)(3) of the Internal Revenue Code, relating to~~  
9 ~~denial of deduction for club dues, shall not apply.~~

10 SEC. 47. Section 24661.3 is added to the Revenue and  
11 Taxation Code, to read:

12 24661.3. (a) (1) The options under Sections 112(d)(2) and  
13 112(d)(3) of the Federal Agriculture Improvement and Reform Act  
14 of 1996 (7 U.S.C. Sec. 7212(d)(2) and (3)), as in effect on October  
15 21, 1998, shall be disregarded in determining the taxable year for  
16 which any payment under a production flexibility contract under  
17 Subtitle B of Title I of that act (as so in effect) is properly includable  
18 in gross income for purposes of this part, Part 10.2 (commencing  
19 with Section 18401), or Part 10 (commencing with Section 17001).

20 (2) In order to provide farmers with the same tax treatment for  
21 all payments in years beginning before January 1, 2002, with  
22 respect to production flexibility contract payments as under  
23 federal law, as modified by P.L. 105-277, this section shall apply  
24 to taxable years ending after December 31, 1995.

25 (b) Any option to accelerate the receipt of any payment under  
26 a production flexibility contract entered into on or after January  
27 1, 2002, which is payable under the Federal Agriculture  
28 Improvement and Reform Act of 1996 (7 U.S.C. Sec. 7200 et seq.),  
29 as in effect on December 17, 1999, shall be disregarded in  
30 determining the taxable year for which that payment is properly  
31 includable in gross income for purposes of this part, Part 10.2  
32 (commencing with Section 18401), or Part 10 (commencing with  
33 Section 17001).

34 SEC. 48. Section 24667 of the Revenue and Taxation Code is  
35 amended to read:

36 24667. (a) (1) Sections 453, 453A, and 453B of the Internal  
37 Revenue Code, relating to installment method, special rules for  
38 nondealers, and gain or loss on disposition of installment  
39 obligations, respectively, shall apply, except as otherwise  
40 provided.



(2) Sections ~~811(c)(2)~~, 811(c)(4), 811(c)(6), and 811(c)(7) of Public Law 99-514, as modified by Section 1008(f) of Public Law 100-647, shall apply to each taxable year beginning on or after January 1, 1988.

(3) Section 812 of Public Law 99-514, relating to the disallowance of use of the installment method for certain obligations, as modified by Section 1008(g) of Public Law 100-647, shall apply to each taxable year beginning on or after January 1, 1988.

(b) For purposes of subdivision (a), any references in the Internal Revenue Code to sections that have not been incorporated into this part by reference shall be deemed to refer to the corresponding section, if any, of this part.

(c) In the case of any taxpayer who made sales under a revolving credit plan and was on the installment method under former Section 24667 or 24668 for the taxpayer's last taxable year beginning before January 1, 1988, the provisions of this section shall be treated as a change in method of accounting for the first taxable year beginning after December 31, 1987, and all of the following shall apply:

(1) That change shall be treated as initiated by taxpayer.

(2) That change shall be treated as having been made with the consent of the Franchise Tax Board.

(3) The period for taking into account adjustments under Article 6 (commencing with Section 24721) by reason of that change shall not exceed four years.

(d) The repeal of Section 453C of the Internal Revenue Code by Section 10202(a) of Public Law 100-203, relating to repeal of the proportionate disallowance of the installment method, shall apply to dispositions on or after January 1, 1990, in taxable years beginning on or after January 1, 1990.

(e) (1) In the case of any installment obligations to which Section 453(l)(2)(B) of the Internal Revenue Code applies, in lieu of the provisions of Section 453(l)(3)(A) of the Internal Revenue Code, the "tax" (as defined by subdivision (a) of Section 23036) for any taxable year for which payment is received on that obligation shall be increased by the amount of interest determined in the manner provided under Section 453(l)(3)(B) of the Internal Revenue Code.

(2) Sections 10202 and 10204 of Public Law 100-203, are modified to provide for each of the following:

(A) Section 10202 shall apply to dispositions in taxable years beginning on or after January 1, 1990.

(B) Section 10204 shall apply to costs incurred in taxable years beginning on or after January 1, 1990.

(C) Any adjustments required by Section 481 of the Internal Revenue Code shall be included in gross income as follows:

(i) Fifty percent in the first taxable year beginning on or after January 1, 1990.

(ii) Fifty percent in the second taxable year beginning on or after January 1, 1990.

(f) (1) The amendments to Section 453A of the Internal Revenue Code made by Section 2004 of Public Law 100-647, relating to special rules for nondealers, shall apply to each taxable year beginning on or after January 1, 1990.

(2) In the case of any installment obligation to which Section 453A of the Internal Revenue Code applies and which is outstanding as of the close of the taxable year, in lieu of the provisions of Section 453A(c)(1) of the Internal Revenue Code, the “tax” (as defined by subdivision (a) of Section 23036) for the taxable year shall be increased by the amount of interest determined in the manner provided under Section 453A(c)(2) of the Internal Revenue Code.

(3) The provisions of Section 453A(c)(3)(B) of the Internal Revenue Code, relating to the maximum rate used in calculating the deferred tax liability, are modified to refer to the maximum rate of tax imposed under Section 23151, 23186, or 23802, whichever applies, in lieu of the maximum rate of tax imposed under Section 1 or 11 of the Internal Revenue Code.

(g) (1) *The last sentence in Section 453A(d)(4) of the Internal Revenue Code, relating to secured indebtedness, shall not apply.*

(2) *This subdivision shall apply to sales or other dispositions occurring on or after January 1, 2002.*

*SEC. 49. Section 24685.5 is added to the Revenue and Taxation Code, to read:*

*24685.5. (a) The amendment made by Section 7001(a) of the Internal Revenue Service Restructuring and Reform Act of 1998 (P.L. 105-206) to Section 404(a)(11) of the Internal Revenue Code,*

1 *regarding determinations relating to deferred compensation, shall*  
 2 *apply to taxable years beginning on or after January 1, 2002.*

3 *(b) In the case of any taxpayer required by the enactment of this*  
 4 *section to change its method of accounting for its first taxable year*  
 5 *beginning on or after January 1, 2002, each of the following shall*  
 6 *apply for purposes of this part, Part 10 (commencing with Section*  
 7 *17001), and Part 10.2 (commencing with Section 18401):*

8 *(1) The change shall be treated as initiated by the taxpayer.*

9 *(2) The change shall be treated as made with the consent of the*  
 10 *Franchise Tax Board.*

11 *(3) The net amount of the adjustments required to be taken into*  
 12 *account by the taxpayer under Chapter 13 (commencing with*  
 13 *Section 24631) shall be taken into account ratably over the*  
 14 *three-taxable-year period beginning with the taxpayer's first*  
 15 *taxable year beginning on or after January 1, 2002.*

16 *SEC. 50. Section 24710 of the Revenue and Taxation Code is*  
 17 *amended to read:*

18 24710. (a) For each taxable year beginning on or after  
 19 January 1, 1997, Section 475 of the Internal Revenue Code,  
 20 relating to mark to market accounting method for securities  
 21 dealers, shall apply, except as otherwise provided.

22 (b) Section 13233(c)(2)(C) of the Revenue Reconciliation Act  
 23 of 1993 (P.L. 103-66), relating to the effective date for changes in  
 24 the mark to market accounting method for securities dealers, is  
 25 modified to provide that the amount taken into account under  
 26 Section 481 of the Internal Revenue Code of 1986 shall be taken  
 27 into account ratably over the five-taxable-year period beginning  
 28 with the first taxable year beginning on or after January 1, 1997.

29 (c) (1) If a taxpayer has, at any time, made an election for  
 30 federal purposes under Section 475(e) of the Internal Revenue  
 31 Code, relating to election of mark to market for dealers in  
 32 commodities, to have Section 475 of the Internal Revenue Code  
 33 apply, Section 475 of the Internal Revenue Code shall apply to that  
 34 dealer in commodities for state purposes, a separate election for  
 35 state purposes shall not be allowed under paragraph (3) of  
 36 subdivision (e) of Section 23051.5, and the federal election shall  
 37 be binding for purposes of this part.

38 (2) If a taxpayer fails to make, or has not previously made, an  
 39 election for federal purposes under Section 475(e) of the Internal  
 40 Revenue Code, relating to election of mark to market for dealers

1 in commodities, to have Section 475 of the Internal Revenue Code  
2 apply, an election under Section 475(e) of the Internal Revenue  
3 Code shall not be allowed for state purposes, Section 475 of the  
4 Internal Revenue Code shall not apply to that dealer in  
5 commodities for state purposes, and a separate election for state  
6 purposes shall not be allowed under paragraph (3) of subdivision  
7 (e) of Section 23051.5.

8 (d) (1) If a taxpayer has, at any time, made an election for  
9 federal purposes under Section 475(f)(1) of the Internal Revenue  
10 Code, relating to election of mark to market for traders in  
11 securities, to have Section 475 of the Internal Revenue Code apply  
12 to a trade or business, Section 475 of the Internal Revenue Code  
13 shall apply to that trader in securities for state purposes with  
14 respect to that trade or business, a separate election for state  
15 purposes with respect to that trade or business shall not be allowed  
16 under paragraph (3) of subdivision (e) of Section 23051.5, and the  
17 federal election shall be binding for purposes of this part.

18 (2) If a taxpayer fails to make, or has not previously made, an  
19 election for federal purposes under Section 475(f)(1) of the  
20 Internal Revenue Code, relating to election of mark to market for  
21 traders in securities, to have Section 475 of the Internal Revenue  
22 Code apply to a trade or business, an election under Section  
23 475(f)(1) of the Internal Revenue Code shall not be allowed for  
24 state purposes with respect to that trade or business, Section 475  
25 of the Internal Revenue Code shall not apply to that trader in  
26 securities for state purposes with respect to that trade or business,  
27 and a separate election for state purposes shall not be allowed  
28 under paragraph (3) of subdivision (e) of Section 23051.5.

29 (e) (1) If a taxpayer has, at any time, made an election for  
30 federal purposes under Section 475(f)(2) of the Internal Revenue  
31 Code, relating to election of mark to market for traders in  
32 commodities, to have Section 475 of the Internal Revenue Code  
33 apply to a trade or business, Section 475 of the Internal Revenue  
34 Code shall apply to that trader in commodities for state purposes  
35 with respect to that trade or business, a separate election for state  
36 purposes with respect to that trade or business shall not be allowed  
37 under paragraph (3) of subdivision (e) of Section 23051.5, and the  
38 federal election with respect to that trade or business shall be  
39 binding for purposes of this part.



(2) If a taxpayer fails to make, or has not previously made, an election for federal purposes under Section 475(f)(2) of the Internal Revenue Code, relating to election of mark to market for traders in commodities, to have Section 475 of the Internal Revenue Code apply to a trade or business, an election under Section 475(f)(2) of the Internal Revenue Code shall not be allowed for state purposes with respect to that trade or business, Section 475 of the Internal Revenue Code shall not apply to that trader in commodities for state purposes with respect to that trade or business, and a separate election for state purposes with respect to that trade or business shall not be allowed under paragraph (3) of subdivision (e) of Section 23051.5.

(f) (1) An election under Section 475(e) or (f) of the Internal Revenue Code made for federal purposes with respect to a taxable year beginning before January 1, 1998, shall be treated as having been made for state purposes with respect to the first taxable year beginning on or after January 1, 1998.

(2) Section 1001(d)(4)(B) of the Taxpayer Relief Act of 1997 (P.L. 105-34), relating to the effective date for election of mark to market by securities traders and traders and dealers in commodities, is modified to provide that the requirement for timely identification shall be treated as timely made for state purposes if that identification is treated as timely made for federal purposes, and the amount taken into account under Section 481 of the Internal Revenue Code of 1986 shall be taken into account ratably over the four-taxable-year period beginning with the first taxable year beginning on or after January 1, 1998.

(g) *In the case of any taxpayer required by the enactment of the act adding this subdivision, which act incorporated by reference the amendments made by Section 7003 of the Internal Revenue Service Restructuring and Reform Act of 1998 (P.L. 105-206) to Section 475 of the Internal Revenue Code for taxable years beginning on or after January 1, 2002, to change its method of accounting for its first taxable year beginning on or after January 1, 2002, then each of the following shall apply for purposes of this part, Part 10.2 (commencing with Section 18401), and Part 10 (commencing with Section 17001):*

(1) *The change shall be treated as initiated by the taxpayer.*

(2) *The change shall be treated as made with the consent of the Franchise Tax Board.*

1 (3) *The taxpayer shall not be required to change its method of*  
2 *accounting until its first taxable year beginning on or after*  
3 *January 1, 2002.*

4 (4) *The net amount of the adjustments required to be taken into*  
5 *account by the taxpayer under Chapter 13 (commencing with*  
6 *Section 24631) shall be taken into account ratably over the*  
7 *three-taxable-year period beginning with the taxpayer's first*  
8 *taxable year beginning on or after January 1, 2002.*

9 SEC. 51. *Section 24942 of the Revenue and Taxation Code is*  
10 *amended to read:*

11 24942. (a) No gain or loss shall be recognized to a  
12 corporation on the receipt of money or other property in exchange  
13 for stock (including treasury stock) of that corporation. No gain or  
14 loss shall be recognized by a corporation with respect to any lapse  
15 or acquisition of an option, *or with respect to a securities futures*  
16 *contract (as defined by Section 1234B of the Internal Revenue*  
17 *Code), to buy or sell its stock (including treasury stock).*

18 (b) For basis of property acquired by a corporation in certain  
19 exchanges for its stock, see Sections 24552 to 24554, inclusive.

20 SEC. 52. *Section 24949.1 of the Revenue and Taxation Code,*  
21 *as added by Chapter 846 of the Statutes of 1961, is amended to*  
22 *read:*

23 24949.1. For purposes of this part, the sale or exchange of  
24 livestock (other than poultry) held by a taxpayer for draft,  
25 breeding, or dairy purposes in excess of the number the taxpayer  
26 would sell if he *or she* followed his *or her* usual business practices  
27 shall be treated as an involuntary conversion to which Sections  
28 24943 to 24949, inclusive, apply if ~~such that~~ livestock ~~are~~ is sold  
29 or exchanged by the taxpayer solely on account of drought, flood,  
30 *or other weather-related conditions.*

31 SEC. 53. *Section 24949.1 of the Revenue and Taxation Code,*  
32 *as amended by Section 98 of Chapter 322 of the Statutes of 1998,*  
33 *is repealed.*

34 ~~24949.1. (a) Section 1033(e) of the Internal Revenue Code,~~  
35 ~~relating to livestock sold on account of drought, is modified by~~  
36 ~~substituting the phrase "on account of drought, flood, or other~~  
37 ~~weather-related conditions" in lieu of the phrase "on account of~~  
38 ~~drought" contained therein.~~

39 ~~(b) This section shall apply to sales and exchanges after~~  
40 ~~December 31, 1996.~~



~~(c) This section shall not apply to taxable years beginning on or after January 1, 1998.~~

SEC. 54. *In order to provide employers and employees with the same tax treatment for all years with respect to meals or lodging furnished for the convenience of the employer as under federal law, amendments made by the enactment of this act, which incorporates by reference the amendments made by Section 5002 of the Internal Revenue Service Restructuring and Reform Act of 1998 (P.L. 105-206) to Section 119 of the Internal Revenue Code, shall apply to taxable years beginning before, on, or after July 22, 1998.*

SEC. 55. *Sections 6001 to 6024, inclusive, of the Internal Revenue Service Restructuring and Reform Act of 1998 (Title VI of P.L. 105-206), Sections 4001 to 4006, inclusive, of the Tax and Trade Relief Extension Act of 1998 (Title IV of Division J of P.L. 105-277) and Sections 311 to 319, inclusive, of the Consolidated Appropriations Act of 2001 (Subtitle B of Title III of P.L. 106-554) enacted numerous technical corrections to provisions of the Internal Revenue Code, the Ticket to Work and Work Incentives Improvement Act of 1999 (P.L. 106-170), the Tax and Trade Relief Extension Act of 1998 (P.L. 105-277), the Internal Revenue Service Restructuring and Reform Act of 1998 (P.L. 105-206), the Taxpayer Relief Act of 1997 (P.L. 105-34), the Small Business Job Protection Act of 1996 (P.L. 104-188), the Uruguay Round Agreements Act (P.L. 103-465), the Omnibus Budget Reconciliation Act of 1993 (P.L. 103-66), the Revenue Reconciliation Act of 1990 (P.L. 101-508), the Technical and Miscellaneous Revenue Act of 1988 (P.L. 100-647), the Tax Reform Act of 1986 (P.L. 99-514), and the Tax Reform Act of 1984 (P.L. 98-369), some of which are incorporated by specific reference into Part 10 (commencing with Section 17001), Part 10.2 (commencing with Section 18401), and Part 11 (commencing with Section 23001) of Division 2 of the Revenue and Taxation Code. Unless otherwise specifically provided, the technical corrections described in the preceding sentence, to the extent that they correct provisions that are incorporated by specific reference into the Revenue and Taxation Code, are declaratory of existing law and shall be applied in the same manner and for the same periods as specified in the Internal Revenue Service Restructuring and Reform Act of 1998 (Title VI of P.L. 105-206), the Tax and*



1 *Trade Relief Extension Act of 1998 (Title IV of Division J of P.L.*  
2 *105-277), and the Consolidated Appropriations Act, 2001*  
3 *(Subtitle B of Title III of P.L. 106-554) or if later, the specified date*  
4 *of incorporation.*

5 *SEC. 56. The amendments made to Section 17731.5 by this act*  
6 *are declaratory of existing law and shall be applied in the same*  
7 *manner and for the same taxable years as the amendments made*  
8 *by Section 6007(f)(2) of the Internal Revenue Service*  
9 *Restructuring and Reform Act or if later, the specified date of*  
10 *incorporation.*

11 *SEC. 57. The amendments made to Section 17751 by this act*  
12 *are declaratory of existing law and shall be applied in the same*  
13 *manner and for the same taxable years as the amendments made*  
14 *by Section 6013(a) of the Internal Revenue Service Restructuring*  
15 *and Reform Act of 1998 (P.L. 105-206) or if later, the specified date*  
16 *of incorporation.*

17 *SEC. 58. The amendments made to Section 18038.5 by this act*  
18 *are declaratory of existing law and shall be applied in the same*  
19 *manner and for the same taxable years as the amendments made*  
20 *by Section 6005(f) of the Internal Revenue Service Restructuring*  
21 *and Reform Act of 1998 (P.L. 105-206) or if later, the specified date*  
22 *of incorporation.*

23 *SEC. 59. Amendments made by the enactment of this act,*  
24 *which incorporates by reference the amendments made by Section*  
25 *3001 of the Tax and Trade Relief Extension Act of 1998 (P.L.*  
26 *105-277) to Sections 332 and 334 of the Internal Revenue Code,*  
27 *shall apply to distributions made on or after January 1, 2002.*

28 *SEC. 60. In order to provide the same tax treatment for all*  
29 *years with respect to the tax treatment of a cash option for qualified*  
30 *prizes as under federal law, as modified by P.L. 105-277:*

31 *(a) Amendments made by the enactment of this act, which*  
32 *incorporates by reference the amendments made by Section 5301*  
33 *of the Tax and Trade Relief Extension Act of 1998 (P.L. 105-277)*  
34 *to Section 451 of the Internal Revenue Code, shall apply to any*  
35 *prize to which a person first becomes entitled after October 21,*  
36 *1998.*

37 *(b) Amendments made by the enactment of this act, which*  
38 *incorporates by reference the amendments made by Section 5301*  
39 *of the Tax and Trade Relief Extension Act of 1998 (P.L. 105-277)*  
40 *to Section 451 of the Internal Revenue Code, shall apply to any*

1 prize to which a person first becomes entitled on or before October  
2 21, 1998, except that in determining whether an option is a  
3 qualified price option as defined in Section 451(h)(2)(A) of the  
4 Internal Revenue Code:

5 (1) Section 454(h)(2)(A)(ii) of the Internal Revenue Code shall  
6 not apply.

7 (2) That option shall be treated as a qualified prize option if it  
8 is exercisable only during all or part of the 18-month period  
9 beginning on July 1, 1999.

10 SEC. 61. Amendments made by the enactment of this act,  
11 which incorporates by reference the amendments made by Section  
12 3001 of the Miscellaneous Trade and Technical Corrections Act of  
13 1999 (P.L. 106-36) to Sections 351, 357, 358, 362, 368, 584, and  
14 1031 of the Internal Revenue Code, shall apply to transfers made  
15 on or after January 1, 2002.

16 SEC. 62. Section 502(d) of the Ticket to Work and Work  
17 Incentives Improvement Act of 1999 (P.L. 106-170), relating to  
18 special rule delaying the claiming of the research credit, shall not  
19 apply.

20 SEC. 63. Amendments made by the enactment of this act,  
21 which incorporates by reference the amendments made by Section  
22 532 of the Ticket to Work and Work Incentives Improvement Act of  
23 1999 (P.L. 106-170), shall apply to any instrument held, acquired,  
24 or entered into, any transaction entered into, and supplies held or  
25 acquired on or after January 1, 2002.

26 SEC. 64. Amendments made by the enactment of this act,  
27 which incorporates by reference the amendments made by Section  
28 534 of the Ticket to Work and Work Incentives Improvement Act of  
29 1999 (P.L. 106-170), which added Section 1260 of the Internal  
30 Revenue Code to Subchapter P of Chapter 1 of the Internal  
31 Revenue Code, shall apply to transactions entered into on or after  
32 January 1, 2002.

33 SEC. 65. Amendments made by the enactment of this act,  
34 which incorporates by reference the amendments made by Section  
35 537 of the Ticket to Work and Work Incentives Improvement Act of  
36 1999 (P.L. 106-170) to Section 170 of the Internal Revenue Code,  
37 shall apply to transfers made on or after January 1, 2002.

38 SEC. 66. In order to provide the same tax treatment under Part  
39 10 (commencing with Section 17001), Part 10.2 (commencing  
40 with Section 18401), and Part 11 (commencing with Section

23001) of Division 2 of the Revenue and Taxation Code, with respect to distributions by a partnership to a corporate partner, each of the following shall apply:

(a) Except as provided in subdivision (b), amendments made by the enactment of this act, which incorporates by reference the amendments made by Section 538 of the Ticket to Work and Work Incentives Improvement Act of 1999 (P.L. 106-170) to Section 732 of the Internal Revenue Code, shall apply to distributions made on or after January 1, 2002.

(b) (1) In the case of a corporation which is a partner in a partnership as of January 1, 2002, the amendment made by Section 538 of the Ticket to Work and Work Incentives Improvement Act of 1999 (P.L. 106-170) to Section 732 of the Internal Revenue Code, shall apply to any distribution made (or treated as made) to that partner from that partnership after June 30, 2002.

(2) (A) Paragraph (1) shall not apply to any distribution unless the partner has made the election under Section 538(b)(2) of the Ticket to Work and Work Incentives Improvement Act of 1999 (P.L. 106-170) to have Section 538(b)(2) of the Ticket to Work and Work Incentives Improvement Act of 1999 (P.L. 106-170) apply for federal purposes to that distribution on the partner's return of federal income tax for the taxable year in which the distribution occurs.

(B) For purposes of subparagraph (A), no separate election shall be allowed under paragraph (3) of subdivision (e) of Section 17024.5 or paragraph (3) of subdivision (e) of Section 23051.5.

SEC. 67. Amendments made by the enactment of this act to Section 24357.9 shall apply to a qualified computer contribution made on or after January 1, 2002.

SEC. 68. In order to provide the same tax treatment under Part 10 (commencing with Section 17001), Part 10.2 (commencing with Section 18401), and Part 11 (commencing with Section 23001) of Division 2 of the Revenue and Taxation Code, with respect to the sale or exchange of livestock sold or exchanged solely on account of flood or other weather-related conditions, the amendments made to Section 24949.1 of the Revenue and Taxation Code, as added by Chapter 846 of the Statutes of 1961, shall apply to taxable years beginning on or after January 1, 1999.

SEC. 69. This act provides for a tax levy within the meaning of Article IV of the Constitution and shall go into immediate

1 effect. Sections 17052.6, 17085, 17140, 17140.3, 17144.5, 17205,  
2 17501, 17551, 23701s, 23705, 23711, and 23712 of the Revenue  
3 and Taxation Code, as amended or added by this act, conform, in  
4 whole or in part, to the changes made by the Economic Growth and  
5 Tax Relief Reconciliation Act of 2001 (Public Law 107-16) to the  
6 Internal Revenue Code and shall be operative with respect to the  
7 same period as the federal law provision to which it conforms.

8 *SEC. 70. This act shall become operative only if Senate Bill*  
9 *No. 657 of the 2001–02 Regular Session is chaptered.*

